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Supreme Court, U.S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1991

CHARLES L. GRIMES,

Petitioner,

v.

JOHN P. MCCARTHY PROFIT SHARING PLAN, VITALINK COMMUNICATIONS CORPORATION, LESLIE DENEND, and NETWORK SYSTEMS CORPORATION,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF DELAWARE

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QUESTIONS PRESENTED

In reviewing, for approval or disapproval, a settlement negotiated by the lawyer for the named plaintiff in a state court class action, what minimum procedural requirements does due process oblige the state court to observe so as to ensure that the absent members of the class were fairly represented, and were they observed in this case?

PARTIES TO THE PROCEEDING

The names of all parties appear in the caption of the case.

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Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF DELAWARE

Charles L. Grimes respectfully petitions the Court for a writ of certiorari to review the judgment of the Supreme Court of Delaware entered in this proceeding on May 19, 1992.

This case follows a common scenario—especially in Delaware—that has grave potential for abuse and should be examined by this Court from a constitutional perspective. In the instant case the scenario ran thus: A corporation announced a proposed transaction. A class action, purportedly on behalf of the stockholders, attacking the transaction was filed in state court against the corporation and other participants in the transaction, alleging state law violations of fiduciary duty. After hasty discovery, a settlement was reached between the defendants and the named plaintiff, under which minor modifications were made

to the transaction, while the named plaintiff's lawyer received "clear sailing" to collect a generous fee (to be paid by the defendants), and purportedly released on behalf of the class members all their claims in respect of the matter. The state court certified the action as a class action with no "opt-out" opportunity, and after notice to the class and opportunity to be heard on the settlement (but not on the class certification), approved the settlement without any inquiry into its *bona fides*—notwithstanding clear indicia that should have led any reasonable person to make such an inquiry. We submit that due process requires such an inquiry.

I. PRELIMINARY MATTERS

A. Opinions Below

Neither the opinion of the court of first instance (the Court of Chancery of Delaware) nor of the court below (the Supreme Court of Delaware) has been reported. They are reprinted as Appendix C and Appendix A respectively.

B. Jurisdiction

The *per curiam* Order of the court below, Appendix A, was entered on April 30, 1992, and its actual judgment or mandate, Appendix E, was issued on May 19, 1992. This Court has jurisdiction to review the judgment below under 28 U.S.C § 1257(a).

C. Constitutional Provision and Rule of Court Involved

The constitutional provision and rule of court involved are U.S. Const. Amendment 14 and Rule 23 of the Rules of the Chancery Court of Delaware. They are printed in Appendices F and G respectively.

II. STATEMENT OF THE CASE

A. Facts Material To the Consideration of the Questions Presented

Petitioner was a stockholder in respondent Vitalink Communications Corporation, a Delaware corporation. In May of 1991 he and other stockholders received a letter dated May 13, 1991, over the signature of Vitalink's Chairman (respondent Denend) on behalf of all its directors, advising that respondent Network Systems Corporation ("NSC") was making a tender offer of $10.50 per share for their stock, transmitting NSC's "Offer To Purchase" and other papers, and recommending that Vitalink stockholders accept the offer and tender their stock. App. H. The letter and enclosed papers made it plain that NSC's goal was to acquire 100% of Vitalink by securing enough stock through the tender offer to be able under Delaware law to "squeeze out" nontendering stockholders by a forced merger.[1]

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[1] The structure of the deal is not important to the issue here presented and we forbear to burden the Court with its minutiae or to burden the Appendix to this Petition with bulky corporate documents and SEC filings. The general outline of the transaction was as follows: NSC formed a wholly-owned subsidiary, NSC Acquisition Corp. ("Acquisition"). Acquisition issued a tender offer, offering to buy shares of Vitalink at $10.50 per share subject to various conditions, including tender of at least a majority of outstanding shares (plus certain shares issuable on the exercise of stock options). After becoming the controlling stockholder of Vitalink, Acquisition would be merged into Vitalink, and Vitalink would continue as a wholly-owned subsidiary of NSC. Vitalink stockholders who did not tender their shares, and who in connection with the merger exercised the appraisal rights of dissenting stockholders under the Delaware Corporation Law, would receive the right to $10.50 per share and could

Petitioner believed the price of $10.50 was too low and did not tender his stock.

The papers sent to stockholders with Denend's May 13 letter had made brief mention of several state court lawsuits opposing the transaction that had been filed in Delaware and California. App. 55a-58a. In the latter part of July 1991—after the merger had been completed, and nearly two months after the purported settlement described *infra* had been entered into—, petitioner and other Vitalink stockholders received in the mail from the Register in Chancery of the Court of Chancery of Delaware a "Notice of Pendency of Class Action, Class Action Determination, Proposed Settlement, Settlement Hearing and Right To Appear" dated July 18. This advised them that a total of four such state actions had been filed in the Court of Chancery of Delaware and three in California; that the Delaware actions had been consolidated, with the

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pursue their appraisal rights under Delaware law.

This procedure was in fact followed. In mid-July petitioner and other non-tendering stockholders received a "Notice of Merger" dated July 11, 1991, advising them that, having acquired approximately 91% of the shares of Vitalink, the NSC subsidiary had merged itself into Vitalink as of July 1, and that they could either take $10.50 per share or seek appraisal of their stock under Delaware law. Petitioner has taken the latter course and has an appraisal action pending.

The deal contained features often found in such arrangements, designed to make it more difficult for a competing acquiror to make an offer. These included a so-called "lockup" option, whereby Acquisition had an option to buy 20% of Vitalink's stock, thus preventing any competitor from acquiring as much as 80%; and a provision under which Vitalink would reimburse NSC's fees and expenses if it terminated the deal for specified reasons.

complaint in one of them—that of respondent John P. McCarthy Profit Sharing Plan against respondents Vitalink, Denend, and NSC—designated as the consolidated complaint; and that a stipulation for settlement of the consolidated action had been agreed to on May 29 and 30, which was later extended to the California actions. The notice further advised that pursuant to Rule 23 of its rules,[2] the Delaware Court of Chancery had certified a class, for purposes of settlement only, consisting in effect of the Vitalink stockholders.[3] The stockholders were advised that a hearing on the settlement before the Delaware Court of Chancery was scheduled for September 16. They were advised that they could object, but were apprised of no right to opt out of the class. The court purported to enjoin them from filing any more actions with respect to the transaction.

The Notice which was sent to the stockholders is reprinted at Appendix J to this Petition. The stipulation embodying the settlement (in its final version, including the California suits), and the order of the Court of Chancery certifying the class and directing that the Notice be sent, are reprinted at Appendices I and B respectively. It will be noted that paragraph 1 of the latter order specifically precluded any right

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[2] Del. Ch. Ct. Rule 23 is substantially identical to Fed. R. Civ. P. Rule 23. It is reprinted at Appendix G.

[3] To be precise, the class was composed of "all record or beneficial holders of common stock [in Vitalink], and their successors in interest, transferees and assigns, immediate and remote, who held shares at any time during the period from and including May 6, 1991 to and including July 1, 1991, . . . excluding defendants, members of their immediate families, nominees and trusts and corporations controlled by them." App. 4a.

to opt out. App. 3a. It will also be noted that, though the settlement was reached on May 29 and 30 and the final document was dated June 10, the parties waited until the latter part of July—after the "squeeze-out" merger had been consummated—to obtain the court's order.

Under the terms of the settlement:—

- Vitalink and the other defendants agreed not to oppose an application by the named plaintiffs' lawyers for a fee (to be paid by Vitalink) of $275,000 plus up to $25,000 in expenses (such an undertaking not to oppose a fee application is known in the trade as a "clear sailing" agreement);
- The class members would release all claims of any kind arising out of or in any way connected with the acquisition[4]; and
- In consideration thereof, the tender offer, scheduled to expire June 10, would be extended to June 20; minor limitations were placed on the "lockup" stock option agreement; a cap was placed on reimbursement of NSC's fees

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[4] The release is drawn in sweeping terms, App. 65a-66a; see also App. 43a-44a, and respondents contend that it releases not only the state law claims which were the subject of the lawsuits, but also claims for damages under the federal securities laws, over which the state court had no jurisdiction. Petitioner and another stockholder have filed a federal securities law action for damages in respect of the transaction in the United States District Court for the Eastern District of Pennsylvania, in which the scope and validity of the release will be tested. That issue is not presented here (except, of course, that if the approval of the settlement was invalid the release is invalid.)

> and expenses by Vitalink if NSC should terminate the merger agreement under certain circumstances; and public announcements of the foregoing—described as "benefits conferred upon the Class," without any explanation as to why they were "beneficial"—would be made as soon as practicable.

App. 83a-84a.

At the hearing on the settlement, the named plaintiff's counsel applied for $275,000 in legal fees and expenses. They submitted nothing, sworn or unsworn, to justify this number. They submitted no time sheets. They offered no specific description of the work they had done, and no information whatever as to who had done the work, when it was done, why it was necessary, what their normal rates were, or what the customary rates for such work might be. The only specific information laid before the court to justify the fee sought was the assertion that "[p]laintiffs' counsel expended over 500 hours in litigation, negotiation, and settlement of this case, and through the present have incurred expenses of over $20,000." App. 90a.

B. Raising and Disposition of the Federal Questions Sought To Be Reviewed

Regarding the "benefits conferred upon the Class" as derisory and the proposed settlement as essentially a sham, petitioner objected to it.[5] Written memoranda were filed (plus one affidavit not here relevant), and

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[5] As did a number of other stockholders. All the objectors were jointly represented and for simplicity we refer herein merely to the petitioner rather than to the objectors as a group.

oral argument was held at a hearing before the Court of Chancery (Chandler, V.C.) on September 16. (Excerpts from the submissions of the named plaintiffs, and of petitioner and other objectors, are at Appendices K and L respectively. Excerpts from the transcript of the hearing are at Appendix M.[6]) The judge announced at the opening of the hearing that he had read "some but not all of the submissions of those who are proposing the settlement," but not the papers in opposition to the settlement filed by petitioner and other opponents. App. 98a.

From the outset, petitioner urged the court to examine the adequacy of the representation the class members had received. "[P]lease, Your Honor," petitioner's counsel asked, "we would ask you to read these—this record, see whether or not you think this record is really fully developed." App. 101a. Contending that the record was insufficiently developed to give the court a basis for approving the proposed settlement, petitioner urged that the court "decline any invitation to approve the defendants' efforts to be rid of this litigation by paying off the plaintiffs' attorneys, providing sham benefits to the class and cutting off forever the ability of the absent members of the class to pursue their rights." App. 91a. As petitioner's counsel put it at oral argument:

> "It enables us to play the game that people have criticized Delaware and its courts for. That is,

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[6] We cite the memoranda and oral argument before the Court of Chancery with respect to the issues presented to that court because they are the only source for such information. There is no complaint or similar formal pleading before the Court of Chancery in a proceeding of this nature.

> 'We'll pay off these guys, pay off the attorneys. We do something that is meaningless, that doesn't cost us a penny, and we know it's not going to affect us, and we are rid of this litigation and we forever bar the class members from suing us, and we get the release as wide as we can.' That's what they did."

App. 99a.

Petitioner pointed to a number of facts that should have raised questions in the minds of any dispassionate observer as to whether the interests of the class had been adequately represented.

One group of such facts revolved around the minimal discovery and other investigation engaged in by counsel for the named plaintiff. Petitioner pointed out that the named plaintiff had taken the depositions of five persons over a three-day period, two of which were less than 100 pages in length and one of which was less than 50, App. 92a; that one of them, the deposition of NSC's chairman and key negotiator, lasted little more than an hour and ran to 44 pages, App. 100a; that in at least one instance, counsel for the *defendants* had filled in a gap in the *plaintiff's* interrogation, App. 100a-101a; that no inquiry at all had been made of Vitalink's chief financial officer, App. 98a; nor had any effort been made to take the deposition of the newest member of the Vitalink board, which would have been a logical move for diligent plaintiff's counsel. App. 101a. Nor had the named plaintiff taken any steps to have an expert in investment banking review the contentions of the company's investment bankers. App. 98a. Petitioner's counsel pointed out that the key deposition of respondent Denend, Vitalink's chairman (which lasted

less than three hours, App. 104a) "look[ed] anything but hostile," that it read "like direct examination," with "an amazing number of questions answered with 'Yes' "; petitioner's counsel suggested that, though "[n]obody would tell me," his "guess is there were talks going on at this point, or maybe there was an agreement in principle at that point, by the time the depositions occurred." App. 101a.

Another group of such facts revolved around the inability of petitioner to get information from named plaintiff's counsel. Petitioner's counsel advised the court that more than two weeks before the hearing, he had asked the named plaintiff's counsel for information in writing about the settlement—when settlement discussions began, when any agreement in principle was reached, when the possibility of a payment to the named plaintiff's counsel was first discussed, how the proposed agreement was supposed to benefit the class, and specifics about the discovery that had been conducted—and that the named plaintiff's counsel had never responded. App. 91a, 94a-97a, 99a. (At oral argument the named plaintiff's lawyer claimed he had told petitioner's counsel to talk to somebody else in his firm about the settlement discussions; but petitioner's counsel had no recollection of any such response. App. 102a.)

Petitioner's urgings, however, were unsuccessful. The court made no effort to inquire into the timing or nature of the settlement discussions, the justification for the requested $275,000, or any other matter bearing on adequacy of representation.

On November 8, 1991, the court issued a Memorandum Opinion approving the settlement, Appendix C, and issued on November 15 its Order and Final

Judgment pursuant thereto. Appendix D. The opinion did not examine the adequacy of representation or address the *bona fides* of the settlement. It did reject—without discussion or analysis—the objectors' contention that the record was not sufficiently developed to allow it to "evaluate the proposed settlement in an informed manner," but only in the context of "a reasonable basis to respond to all of the asserted claims"—*i.e.*, the substantive merits of the settlement. App. 38a. It commented that the plaintiff's attorney's assertion at oral argument that he had told the objectors' attorney to call someone else at his office about unanswered questions "adequately responded" to the objection that plaintiff's attorneys refused to provide requested information, App. 40a (notwithstanding the fact that, as noted *supra*, the objectors' attorney recalled no such conversation).

The bulk of the opinion was devoted to evaluation of the settlement on the merits under Delaware law. The court found at least one instance in which counsel for the named plaintiffs had misrepresented the record. App. 20a and note 1. It found that a "cloud of doubt" which the Vitalink board should have "*fully* accounted for" remained on Vitalink's investment banker's valuation analysis. App. 25a-26a (emphasis original). Most significantly, it found that the supposed benefits conferred on the class by the settlement were merely "speculative." App. 38a, 40a. Nevertheless, it approved the settlement.

It also approved the full $275,000 fee requested, with brief references to the conventional standards applicable to all fee determinations: "the contingent nature of the fee, the quality of legal services, the standing and ability of counsel, and the public policy

considerations," but with no inquiry into the origin of the $275,000 figure nor any analysis of why that amount rather than some other amount was appropriate. App. 41a.

An order was entered accordingly, approving the settlement and purporting to foreclose further actions in the same all-embracing terms as the release. Appendix D.

Petitioner (and the other objectors) appealed to the Supreme Court of Delaware, the court below. Aside from urging errors of substantive state law committed by the Chancery Court, petitioner reemphasized the factors suggesting that the proposed settlement was a "sham," "grossly unfair to the shareholders who are being forced to relinquish their fundamental due process rights to pursue their claims in exchange for the truly frivolous consideration offered." App. 103a.[7] Petitioner pointed again to the fact that "the critical deposition of [Vitalink's chairman, respondent Denend] lasted less than three hours and shows no sign of credible adversarial effort. Of the four Vitalink directors, [the chairman]'s deposition was one of only two taken. One director, who had been on the board only since March, 1991, was passed over." App. 104a.

At oral argument, the named plaintiff's counsel said that his decision that he had a weak case came to him "within the space of the depositions." App. 105a. Petitioner's counsel pointed out that this was an extraordinarily narrow "space"—that evidently named

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[7] We refer to the briefs (and oral argument) before the court below because under its procedure there is no other way of bringing errors to its attention. Its rules do not provide for assignments of error or other formal pleadings.

plaintiff's counsel's conclusion that a lawsuit "that's based on a press release, that can't wait to be pushed into the courthouse door, with all this merit, all of a sudden has no merit . . . was reached after three days of depositions," and that "[t]he two CEOs of the acquiring and acquired company—I would consider certainly the principals in the negotiation—were both scheduled for deposition the same day. Both were done before lunch time." App. 106a. "[M]y clients," he urged, "were theoretically represented in the lawsuits that were pending. In reality, we certainly were not represented." *Ibid.*

"Under these circumstances," contended petitioner, "it is doubtful whether foreclosure at this time of the shareholders' claims would meet minimal constitutional requirements, let alone Delaware standards of fairness. *See In Re Real Estate Title and Settlement Services Litigation*, 869 F.2d 760, 769 (3d Cir.), *cert. denied*, 493 U.S. 821 (1989). This settlement meets neither standard and the decision validating it should be reversed." App. 104a. The *Real Estate Title* citation was to the Third Circuit's recent reference to this Court's fundamental holding, in *Hansberry* v. *Lee*, 311 U.S. 32 (1940), that "it would violate due process to bind an inadequately represented absent party to a prior judgment."[8]

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[8] That the federal constitutional aspect of what the Court of Chancery had failed to do was first raised on appeal to the court below is no impediment to this Court's jurisdiction. This is not a case where a constitutional issue, such as the validity of a state statute or the action of a state official, was before the court of first instance from the outset. The issue of adequate representation was first enlarged to constitutional dimensions by the Court of Chancery's failure even to examine petitioner's

In a brief *per curiam* order, the court below affirmed the Court of Chancery "on the basis of and for the reasons assigned by the Court of Chancery in its well-reasoned memorandum opinion dated November 8, 1991 and its order and final judgment dated November 15, 1991." Appendix A.

III. REASONS FOR THE ALLOWANCE OF THE WRIT

A. The Question Presented Is an Important Question of Federal Law Which Has Not Been, But Should Be, Settled by This Court

1. This Court Can Eliminate a Serious Risk of Grave Abuse by Specifying Minimum Standards for Examining the Adequacy of Representation in State Class Action Settlements

More than fifty years ago, in *Hansberry* v. *Lee*, 311 U.S. 32 (1940), this Court established the bedrock substantive proposition that due process will not allow a state court to bind absent class members in a class action unless they are adequately represented.

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contention that the settlement was a sham. Especially given the fact that, as the Court of Chancery recognized, App. 16a, Delaware law imposes on the court reviewing a class action settlement the obligation to exercise its own independent business judgment, acting on behalf of the absent class members and seeking to protect and advance their interests—an obligation which, as the Court of Chancery noted, is further heightened where, as here, the class members were afforded no opportunity to opt out—petitioner had no reason to expect such a total failure to act on the part of the trial court. (Even if it had been appropriate to raise the constitutional aspect in the Court of Chancery, the rules of the court below are explicit that where the interests of justice require, it may consider and determine questions not presented to the trial court. R. Del. Sup. Ct. Rule 8.)

The intervening half-century, and especially the quarter century since the 1966 amendments to Fed. R. Civ. P. Rule 23 and the subsequent adoption of similar state rules, has seen an explosive growth of class action activity.

Yet we are not aware that this Court has ever fleshed out the *substantive* principle of *Hansberry* v. *Lee* by defining the *procedural* minimum that a court should undertake to satisfy itself that the class is adequately represented.

Most class actions, of course, are settled. The potential for abuse in such settlements by a "sellout" on the part of the named plaintiff is well-recognized. *E.g.*, Borden, *The Shareholder Suit Charade: The Wilmington Filers Shake Down Corporations in Delaware and Nobody Seems To Mind*, AM. LAWYER (Dec. 1989) 67; Coffee, *Understanding the Plaintiff's Attorney: The Implications of Economic Theory for Private Enforcement of Law Through Class and Derivative Actions*, 86 COLUM. L. REV. 669, 714-20 (1986); Coffee, *The Unfaithful Champion: The Plaintiff As Monitor in Shareholder Litigation*, 48 LAW & CONTEMP. PROBS. (Summer 1985) 5, 26-33; Coffee, *Rescuing the Private Attorney General: Why the Model of the Lawyer as Bounty Hunter Is Not Working*, 42 MD. L. REV. 215, 232-33, 239-46 (1983); see Alexander, *Do the Merits Matter? A Study of Settlements in Securities Class Actions*, 43 STANFORD L. REV. 497, 597 (1991). That potential is particularly marked in cases like the present one, where the first plaintiff to reach the state courthouse sells a plenary indulgence to corporate management. By the same token, it is particularly appropriate for this Court to specify minimum procedural standards for ascertaining the *bona fides*

of such arrangements—just as it did not hesitate to specify minimum procedural standards for state class actions seeking to bind non-resident plaintiff class members in *Phillips Petroleum Co.* v. *Shutts*, 472 U.S. 797, 812 (1985).

And this case is a particularly suitable vehicle for that purpose. Few cases will combine so many clues suggesting a sham transaction:

- A settlement negotiated before the class was certified (*cf. County of Suffolk* v. *Long Island Lighting Co.*, 907 F.2d 1295 (2d Cir. 1990); *Weinberger* v. *Kendrick*, 698 F.2d 61, 72-73 (2d Cir. 1982), *cert. denied*, 464 U.S. 818 (1983);

- Attorney's fees negotiated as part of the settlement negotiations[9];

- A "clear sailing" agreement as to the fee[10];

- A fee paid by the defendants to the named plaintiff's lawyers, amounting by those lawyers' own admission to at least $500 an hour;

- Only a vague unsworn description of why the amount of the fee sought was appropriate, and no evidence to compare it with other fees of

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[9] Though not always improper standing alone, see *Evans* v. *Jeff D.*, 476 U.S. 717 (1986), such timing is a factor which should have put the court on inquiry when taken together with the other factors presented here.

[10] "We believe it to be self-evident that the inclusion of a clear sailing clause in a fee application should put a court on its guard, not lull it into aloofness." *Weinberger* v. *Great Northern Nekoosa Corp.*, 925 F.2d 518, 525 (1st Cir. 1991) (footnote omitted).

the same or similar lawyers in the relevant marketplace[11];

- Evasiveness, or downright stonewalling, when petitioner tried to find out when the fee deal was made, and sought other relevant additional information;
- Only modest discovery conducted by the named plaintiff's lawyers, which at least once was supplemented by the *defendants'* lawyer;
- A settlement which the court found to confer only "speculative" benefits on the class; and
- A sweeping release purporting to protect the defendants against all claims of whatever kind by any class member in respect of the transaction.

Courts, it has often been said, must not blind themselves as judges to what they know as men and women. Even the least cynical man or woman, contemplating these circumstances, must conclude that it is at least possible that something irregular has taken place; that "the scenario was such as to suggest, strongly, that the fee arrangement"—and hence the whole settlement—"be placed under the microscope of judicial scrutiny." *Weinberger* v. *Great Northern Nekoosa Corp.*, *supra*, 925 F.2d at 525.

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[11] Contrast the requirements for determining a reasonable attorney's fee under 42 U.S.C. § 1988 laid down by this Court in *Hensley* v. *Eckerhart*, 461 U.S. 424, 433-37 (1982): consideration of hours expended and reasonable hourly rates (sometimes called the "lodestar"), evidence supporting hours worked and rates claimed, exclusion of hours not reasonably expended, level of success achieved, work expended on specific claims, etc.

Yet in the case at bar the court, confronted with these circumstances, put its head into the sand. Though it described itself as held to a high standard, "act[ing] on behalf of the absent class members and seek[ing] to protect and advance their interests," App. 16a, it made no inquiry into when the deal had been cut, why the $275,000 sought by the named plaintiff's lawyers was reasonable, or any of the other questions that would naturally occur to any observer. It simply approved the deal and purportedly cut off all rights of the absent class members.

We submit that due process requires more than that. Just as in a reorganization proceeding "[t]here can be no informed and independent judgment as to whether a proposed compromise is fair and equitable until the bankruptcy judge has apprised himself of all facts necessary for an intelligent and objective opinion," *Protective Committee* v. *Anderson*, 390 U.S. 414, 424 (1968), in a proposed class settlement there can be no "informed and independent judgment" as to adequacy of representation if the judge does not "apprise[ ] himself of all facts necessary for an intelligent and objective opinion." We submit that, at least where, as here, circumstances come to the court's attention that would place a reasonable person on inquiry as to whether absent class members have been adequately represented in connection with a settlement, due process requires the court to develop an evidentiary record from which the question of adequate representation can fairly be appraised, and to demonstrate that it has given that record due consideration, before taking action which purports to cut off forever the rights of absent class members.

We emphasize that we do not suggest that this Court inquire at this time into whether there was *in fact* adequate representation below. Our whole point is that that has not yet been litigated: that the courts below failed to develop a record from which that judgment can be made. The trial court's opinion is devoted almost entirely to an exposition of its "business judgment" with respect to the settlement, under the Delaware rule. But the Chancellor's business judgment is no substitute for adequacy of representation.

2. It Is Appropriate for This Court To Decide This Question Now, Rather Than in a Subsequent Collateral Attack on the Settlement Approved Below.

Hansberry v. *Lee*, *supra*, has a second fundamental teaching: that a class action judgment is always open to collateral attack in another proceeding on the part of a class member who contends that it cannot constitutionally bind him. And, indeed, the issue here presented will be one of the grounds on which the plaintiffs in the action in the Eastern District of Pennsylvania alluded to in note 4 *supra* will contend that the settlement does not bar that action.

We submit that nevertheless it is appropriate for the Court to address the question now. As White, C.J., said long ago in *Riverside Mills* v. *Menefee*, 237 U.S. 189, 197 (1915): "The [full faith and credit and due process] clauses are harmonious and because the one may be applicable to prevent a void judgment being enforced affords no ground for denying efficacy to the other in order to permit a void judgment to be rendered." Even an invalid class settlement puts a cloud on the rights of absent class members; if collateral attack gave sufficient protection against that cloud, there would be no need for Rule 23(e).

More to the present point, all that is at issue here is whether the *procedure* followed by the courts below was proper. The record on that issue is as fully developed now as it can ever be. Discovery in the Eastern District of Pennsylvania will no doubt develop an abundant record as to the merits of a contention of inadequate representation, including the timing and nature of the settlement negotiations; but it can add nothing to knowledge of what the courts below actually did.

Moreover, it could take years for the issue finally to wend its way up to this Court from the Eastern District of Pennsylvania. Meanwhile, the steady flow of class action settlements will continue, and not merely in Delaware. Guidance from this Court will govern not only all such proceedings but also any proceedings in which settlements are collaterally examined on similar grounds. We submit that the courts should have this Court's guidance on this matter now rather than later.

CONCLUSION

The defendants are now seemingly "vaccinated" against all claims; the named plaintiff's lawyer has taken home a large fee paid by the defendants; and the other stockholder class members are left seemingly stripped of all claims with respect to the matter, in exchange for modifications to the transaction which even the state court found to be of only "speculative" benefit to them. Yet the courts below gave no consideration to the *bona fides* of the transaction notwithstanding a number of circumstances that should at least have put them on inquiry.

This all-too-common scenario warrants this Court's attention. The petition for writ of certiorari should be granted.

Respectfully submitted,

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202-223-9010
Attorney for Petitioner
(Counsel of Record)

June 29, 1992

APPENDIX

APPENDIX A

Opinion (Order) of the Supreme Court of Delaware

IN THE SUPREME COURT OF THE STATE OF DELAWARE

No. 468, 1991

Court Below—Court of Chancery of the State of Delaware, in and for New Castle County
C.A. No. 12085

CHARLES L. GRIMES, JOHN D. BURTON, REED RUBIN, LOUISE I.G. IRELAND, RENATE WINSTON (as custodian for HELLA WINSTON), WILLIAM P. WOOD, JR., LOUISA W. RUBY, CHARLES KELLY, GADFLY FOUNDATION, INC. and FIDELITY BANK (as custodian for GORDON W. CHAPLIN and for SUSAN C. STERNBERG),

Objectors Below,
Appellants,

v.

JOHN P. McCARTHY PROFIT SHARING PLAN,

Plaintiff Below,
Appellee.

and

VITALINK COMMUNICATIONS CORPORATION, LESLIE DENEND and NETWORK SYSTEMS CORPORATION,

Defendants Below,
Appellees.

Submitted: April 28, 1992
Decided: April 30, 1992

Before **HORSEY, MOORE and HOLLAND,** Justices.

ORDER

This 30th day of April, 1992, the Court having considered this matter after oral argument and upon the briefs filed by the parties, and having concluded that the same should be affirmed on the basis of and for the reasons assigned by the Court of Chancery in its well-reasoned memorandum opinion dated November 8, 1991 and its order and final judgment dated November 15, 1991.

NOW, THEREFORE, IT IS HEREBY ORDERED that the judgment of the Court of Chancery be, and the same hereby is,

AFFIRMED.

BY THE COURT:

/s/ Randy J. Holland
Justice

APPENDIX B

Order of the Court of Chancery of Delaware With Respect to Class Certification and Settlement Hearing

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

Consolidated
C.A. No. 12085

IN RE VITALINK COMMUNICATIONS CORPORATION SHAREHOLDERS LITIGATION

ORDER

The parties to the above-captioned consolidated action (the "Consolidated Action"), having applied for an Order seeking a class action determination and having entered into the Stipulation and Agreement of Compromise, Settlement and Release, dated June 10, 1991 (the "Stipulation" or the "Settlement"), which, among other things, seeks dismissal of the Consolidated Action upon the terms and conditions set forth in the Stipulation;

NOW, upon the consent of the parties, after consideration of the Stipulation filed with the Court and the exhibits annexed thereto, and after due deliberation, IT IS HEREBY ORDERED THAT:

1. Pursuant to Court of Chancery Rules 23(a) and 23(b)(1) and/or (b)(2), the Consolidated Action, for purposes of the Settlement only, shall be maintained as a class action, without the right of members of the class to opt out, by the named plaintiffs as class representatives and by their counsel as class counsel on behalf of a class con-

sisting of all record or beneficial holders of common stock of Vitalink Communications Corporation ("Vitalink"), and their successors in interest, transferees and assigns, immediate and remote, who held shares at any time during the period from and including May 6, 1991 to and including July 1, 1991, the effective date of the Merger (as defined in the Stipulation), excluding defendants, members of their immediate families, nominees and trusts and corporations controlled by them (the "Class").

2. A hearing shall be held on Sept. 16, 1991, at 11:30 a.m., at the Public Building, 11th and King Streets, Wilmington, Delaware, to (a) determine whether the Settlement should be approved by the Court, (b) determine whether judgment should be entered pursuant to the Stipulation, among other things, dismissing the Consolidated Action with prejudice, (c) rule on application of plaintiffs' counsel for attorneys' fees and reimbursement of expenses, and (d) rule on such other matters as the Court may deem appropriate.

3. The Court reserves the right to adjourn the hearing or any adjournment thereof without further notice of any kind other than oral announcement at the hearing or any adjournment thereof.

4. A notice of the hearing in substantially the form annexed hereto as Appendix A (the "Notice to the Class") shall be mailed by Vitalink within 14 days of the date of this Order to all Class members appearing in the transfer journals of Vitalink as record owners of Vitalink common stock from May 6, 1991 through July 1, 1991 at their last known addresses. The Notice to the Class shall request that such record owners forward the Notice to the Class to the beneficial holder of such shares of Vitalink common stock if any person other than the record owner was the beneficial holder of such shares. Vitalink shall also use reasonable efforts to give notice to such beneficial owners of Vitalink common stock by making additional copies of

the Notice to the Class available to any record holder who, prior to the hearing, requests them for distribution to beneficial owners.

5. The Court reserves the right to approve the Settlement with or without modification and with or without further notice of any kind.

6. The form and method of notice specified herein is the best notice practicable and shall constitute due and sufficient notice of the hearing to all persons entitled to receive such notice. Vitalink shall, at or before the hearing directed herein, file an appropriate affidavit with respect to preparing and mailing the Notice to the Class.

7. Any member of the Class who objects to the Settlement and/or judgment to be entered herein, the application for attorneys' fees and expenses or who otherwise wishes to be heard, may appear in person or by his attorney at the hearing and present evidence or argument that may be proper and relevant; provided, however, that no person other than counsel for the named plaintiffs and defendants shall be heard and no papers, briefs, pleadings or other documents submitted by any person shall be considered by the Court unless not later than 10 days prior to the hearing such person files with the Court and serves upon counsel listed below: (a) a written notice of intention to appear; (b) a statement of such person's objections to any matter before the Court; and (c) the grounds therefor or the reasons that such person desires to appear and be heard, and all documents or writings which such person desires the Court to consider. Copies of all such papers shall be served upon the following counsel:

Joseph A. Rosenthal, Esquire
Morris, Rosenthal, Monhait & Gross, P.A.
First Federal Plaza
P.O. Box 1070
Wilmington, Delaware 19899

Arthur N. Abbey, Esquire
Abbey & Ellis
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New York, New York 10016

Lester Levy, Esquire
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845 Third Avenue
New York, New York 10022

Randolph K. Herndon, Esquire
Skadden, Arps, Slate, Meagher & Flom
One Rodney Square
P.O. Box 636
Wilmington, Delaware 19899

Bruce M. Stargatt, Esquire
Young, Conaway, Stargatt & Taylor
11th Floor, Rodney Square North
P.O. Box 551
Wilmington, Delaware 19899

8. Pending final determination of whether the Stipulation should be approved, plaintiffs, all members of the Class, or any of them, either directly, representatively or in any capacity, upon receipt of the Notice to the Class, shall not commence or prosecute any action asserting any claims which are or relate to the Settled Claims (as defined in the Stipulation).

9. If the Settlement is not approved by the Court or shall not become effective for any reason whatsoever, the Settlement (including any modification thereof made with the consent of the parties as provided for in the Stipu-

lation), any class certification herein and any actions taken or to be taken in connection therewith (including this Order and any judgment entered herein) shall be terminated and shall become void and have no further force and effect, except for Vitalink's obligation to pay the costs of providing the Notice to the Class provided for in paragraphs E(4) and J of the Stipulation.

/s/ William B. Chandler III
Vice Chancellor

Dated: July 18, 1991

CONSENTED TO:

/s/ Joseph A. Rosenthal
Joseph A. Rosenthal, Esquire
Morris, Rosenthal, Monhait
& Gross, P.A.
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Attorneys for Defendant Network
Systems Corporation

/s/ Bruce M. Stargatt
by Bruce L. Silverstein
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Attorneys for Defendant Vitalink
Communications Corporation and
Leslie G. Denend

[Appendix A (Notice to the Class) omitted; see Appendix J hereto]

APPENDIX C

Memorandum Opinion of the Court of Chancery of Delaware

**IN THE COURT OF CHANCERY
OF THE STATE OF DELAWARE
IN AND FOR NEW CASTLE COUNTY**

**Consolidated
Civil Action No. 12085**

IN RE VITALINK COMMUNICATIONS CORPORATION SHAREHOLDERS LITIGATION

MEMORANDUM OPINION

**Date Submitted: September 16, 1991
Date Decided: November 8, 1991**

Joseph Rosenthal, Esquire, of ROSENTHAL, MONHAIT & GROSS, P.A., Wilmington, Delaware; ABBEY & ELLIS, New York, New York, Attorneys for Plaintiffs.

Steven J. Rothschild, Esquire, Randolph K. Herndon, Esquire, and Robert A. Glen, Esquire, of SKADDEN, ARPS, SLATE, MEAGHER & FLOM, Wilmington, Delaware; Bruce M. Stargatt, Esquire, and Bruce L. Silverstein, Esquire, of YOUNG, CONAWAY, STARGATT & TAYLOR, Wilmington, Delaware; Boris Feldman, Esquire, of WILSON, SONSINI, GOODRICH & ROSATI, Palo Alto, California, Attorneys for Defendants.

Gregory P. Williams, Esquire, J. Michael Christopher, Esquire, and Helen M. Richards, Esquire, of RICHARDS, LAYTON & FINGER, Wilmington, Delaware, Attorneys for Objectors.

CHANDLER, Vice Chancellor

Plaintiff, John P. McCarthy Profit Sharing Plan, was a shareholder of Vitalink Communications Corporation ("Vitalink"). On May 9, 1991, plaintiff, alleging breaches of fiduciary duties and the aiding and abetting of the breaches, instituted a class action suit on behalf of all Vitalink common stockholders who were to have their equity interests in Vitalink eliminated because of its merger with Network Systems Corporation ("NSC"). The defendants in this case are Vitalink, Leslie Denend, who was Chief Executive Officer, President and Director of the Vitalink Board of Directors (the "Board") and NSC.

Plaintiff and defendants filed a Stipulation and Agreement of Compromise, Settlement and Release (the "Settlement Agreement") with this Court on July 16, 1991. On July 18, I entered an Order (i) certifying a class of Vitalink's shareholders for the purpose of the settlement and (ii) approving the Notice of Pendency of Class Action, Class Action Determination, Proposed Settlement, Settlement Hearing and Right to Appear (the "Notice"). Pursuant to the Order, the parties mailed the Notice to the members of the class on July 29, 1991.

On September 6, 1991, Charles L. Grimes, John D. Burton, Reed Rubin, Louise I. G. Ireland, Renate Winston (as custodian for Hella Winston), William P. Wood, Jr., Louisa W. Ruby, Charles Kelly, Gadfly Foundation, Inc., Fidelity Bank (as custodian for Gordon W. Chaplin and as custodian for Susan C. Steinberg) (collectively, the "Objectors") filed an objection and a memorandum in opposition to the proposed settlement. On September 16, I held a hearing to determine whether I should approve the Settlement Agreement. This is my decision as to whether I approve the Settlement Agreement.

Part I of this Opinion gives a brief factual history. Part II delineates the class action approval standard. Part III discusses the probable validity of the claims. Part IV

weighs the value of the claims against the value of the settlement. Part V discusses plaintiff's request for lawyers' fees and expenses. Finally, part VI states my conclusions.

I. FACTUAL HISTORY

Vitalink was a corporation duly organized under Delaware law with its principal offices located in Fremont, California. Vitalink was a high-technology company that designed, manufactured, marketed and supported data communications products known as wide area bridges. Vitalink experienced tremendous growth in the late 1980s. By the end of 1989, Vitalink controlled approximately 70 percent of the market and had developed close relationships with many of its 1500 customers.

In early 1990, Vitalink's competitive outlook began to deteriorate. Routers, rather than bridges, became the more desirable interconnect product for many of Vitalink's customers. Vitalink's stock "tumbled from $17 in mid-February to $11 [per share] by the end of the month." (Def. Exh. 15 at N200316.)

In February 1990, the Board engaged Kidder, Peabody & Co., Inc. ("Kidder") to assist in exploring Vitalink's financial and strategic alternatives to the industry's changes. By late April, Kidder had prepared a draft Offering Memorandum that Vitalink would have delivered to any party interested in purchasing it, if it had been finalized. In April 1990, Vitalink instructed Kidder to suspend its efforts related to the exploration of Vitalink's strategic and financial alternatives.

In late October 1990, the Board hired Leslie G. Denend as its new Chief Executive Officer and President. An independent executive search firm had located Denend. Denend had no previous affiliation or financial interest with Vitalink. The Board instructed Denend to familiarize himself with Vitalink, explore the company's alternatives and report his findings.

On December 10, 1990, Denend first met with NSC. NSC is a corporation that designs, manufactures and services high performance data communications equipment which connects mainframe computers, minicomputers and workstations. At the conclusion of this meeting, Denend believed that all business combination discussions with NSC had ended and that NSC would not contact Vitalink again. (Denend Dep. at 13, 29.)

In mid January 1991, Vitalink representatives held a phone conversation with NSC about the possibilities of an original equipment manufacturer ("OEM") relationship. (Denend Dep. at 29.) The proposed relationship would attempt to maximize the value of NSC's router technology and Vitalink's distribution network.

In late January or early February 1991, Vitalink began to hold discussions with another company ("A Co."). (Denend Dep. at 34, 39.) Following this meeting with A Co., Denend held another meeting with NSC. (Denend Dep. at 30.) The topic of this meeting was NSC technology that possibly could be used in an OEM relationship. At the conclusion of this meeting, Denend believed that NSC would not make a proposal for the acquisition of or a business combination with Vitalink. (Denend Dep. at 35, 36.)

On February 12, 1991, Vitalink held a board meeting. At this meeting, the Board considered the possibility of executing change in control employment agreements (the "Control Agreements") with its key employees. (Denend Exh. 4 at V0004172.) Also, Denend summarized his view of Vitalink's business alternatives. (*Id.*)

After this board meeting, Vitalink representatives also held discussions with another company ("B Co."). In all, Vitalink held two meetings and a phone conversation with B Co. Ultimately, B Co. decided that the pursuit of a business combination with Vitalink was not in its best interests because of its goal to pursue an initial public

offering. (Denend Dep. at 20.) B Co. revealed its decision to Vitalink by March 25, 1991. (Valdez Dep. at 64-65.)

On March 5, 1991, Denend signed his Control Agreement. (Denend Exh. 3.) On March 15, 1991, Vitalink met with NSC again. It was at this meeting that Vitalink and NSC decided that an OEM relationship would not be the best way to exploit their respective strengths. (Valdez Dep. at 56; Altman Dep. at 13; Def. Exh. 16 at VA0003517.) Also during March, Vitalink rehired Kidder to explore its strategic alternatives.

In this same time frame (*i.e.*, early spring 1991), Vitalink continued to discuss a possible business combination with A Co. Ultimately, A Co. desired to have a three-way combination with A Co., Vitalink and a third party ("C Co."). Denend believed that such a transaction would take about eight to twelve months to consummate. (Denend Dep. at 21.)

During March and April 1991, Vitalink continued its discussions with NSC. The parties focused their attention on the possibility of a business combination and its form and structure since they had decided that an OEM relationship would not be the most valuable way to structure the relationship between the two entities. (Denend Dep. at 52-53, 58-59, 62.) At the April 9, 1991 Vitalink board meeting, the Board considered the possibility of a business combination with NSC and its probable advantages and disadvantages. (Def. Exh. 24 at VA004212.)

Between April 9 and April 23, Kidder conducted its due diligence as to a possible Vitalink/NSC business combination. On April 23, 1991, the Vitalink Board held a meeting where it determined that it was not realistic to expect another bidder to surface given the outcome of negotiations with A Co., B Co. and C Co. (Def. Exh. 26 at VA004239.) Thus, the Board requested NSC to make a concrete bid. (*Id.* at VA004240.)

Shortly after the Board's April 23 meeting, NSC made its first bid for Vitalink. The offer was a market offer. That is, it basically was an offer to purchase Vitalink at its trading price. The bid was for $7.40 cash and $1 of NSC common stock. Also, NSC conditioned the offer on Vitalink granting NSC an option to buy 19.9% of Vitalink's common stock (the "Lockup"), Vitalink agreeing to not solicit alternative offers ("the "No-Shop") and certain Vitalink officers agreeing to enter into new employment agreements with NSC. At the April 29, 1991 board meeting, the Vitalink Board rejected the offer. (Def. Exh. 25 at VA004244.)

On May 1, 1991, NSC made a second offer to buy Vitalink. NSC increased the consideration offered so as to give a small premium ($.20-$.25 per share). Again, the Board rejected NSC's offer as inadequate.

On May 1, 1991, NSC made a third offer to buy Vitalink. Pursuant to this bid, NSC offered to purchase all Vitalink common stock for $10.50 cash per share. Also, it was subject to the conditions discussed above as applying to the first offer (*i.e.*, the Lockup, No-Shop and employment agreements). On May 5 and 6, the Board met to consider this third offer. On May 6, 1991, the Board accepted NSC's offer, recommended it to Vitalink's stockholders and publicly announced the transaction. The May 6, 1991 closing trading price for Vitalink was $8.50 per share. Thus, the $10.50 offer represented approximately a 23.5% premium over Vitalink's market price.

On May 9, 1991, plaintiff filed this suit with this Court. Pursuant to the terms of the offer, NSC commenced the tender offer on May 13. On May 29-30, the parties executed the Settlement Agreement. The purported consideration given to plaintiff and the class for the execution of the Settlement Agreement was: (1) NSC extended the tender offer for ten days so that it would not close until June 20, 1991; (2) the parties amended their merger agree-

ment so that Vitalink's reimbursement of NSC's fees and expenses was limited to $1.75 million, (3) the parties amended the Lockup so as to limit the cancellation amount payable to NSC to $2,771,331 (the number of Lockup shares multiplied by $1 per share); and (4) the parties agreed to publicly announce the extension of the tender offer and the amendments to their merger agreement and the Lockup.

The tender offer expired on June 20, 1991. At the close of the tender offer, NSC owned approximately 90.7% of Vitalink. The parties consummated the merger on July 1 by performing a short form merger. *See* 8 *Del. C.* § 253. On July 11, 1991, NSC mailed notice to the former stockholders of Vitalink who had not tendered their shares informing them of the consummation of the merger.

As described above, the parties filed the Settlement Agreement with the Court on July 16, 1991. On July 18, I entered an Order certifying a class for the purpose of the settlement and approving the Notice to the class. Pursuant to the Order, the parties mailed the Notice to members of the class on July 29. On September 6, 1991, the Objectors filed an objection and a memorandum in opposition to the proposed settlement. Finally, on September 16, I held a hearing to determine whether I should approve the Settlement Agreement.

II. CLASS ACTION SETTLEMENT APPROVAL STANDARD

As a general matter, Delaware courts have favored the voluntary settlement of lawsuits. *See, e.g., Nottingham Partners v. Dana*, Del. Supr., 564 A.2d 1089, 1102 (1989); *Polk v. Good*, Del. Supr., 507 A.2d 531, 535 (1986); *Rome v. Archer*, Del. Supr., 197 A.2d 49, 53 (1964); *Braun v. Fleming-Hall Tobacco Co., Inc.*, Del. Supr., 92 A.2d 302, 309-310 (1952). Further, Delaware courts have favored the settlement of class actions in particular because the set-

tlements promote the interest of judicial economy. *See generally In re MAXXAM Group, Inc. Stockholders Litig.*, Del. Ch., C.A. No. 8636, Allen, C. (Apr. 16, 1987), slip op. at 2; *Amsellem v. Shopwell, Inc.*, Del. Ch., C.A. No. 5683, Hartnett, V.C. (Sept. 6, 1979), slip op. at 5.

As far as the standard that I must use in deciding whether to approve the settlement, this Court consistently has held that:

> [a] motion of this sort requires the court to exercise a judgment of its own as to the fairness and adequacy of the proposed settlement. *Polk v. Good*, Del. Supr., 507 A.2d 531 (1986); *Rome v. Archer*, Del. Supr., 197 A.2d 49 (1964). In doing so, the court acts on behalf of the absent class members and seeks to protect and advance their interests . . . . The burden rests upon those proposing the settlement to persuade the court that it is fair and reasonable in all of the circumstances.

In re Amsted Industries Inc. Litig., Del. Ch., Cons. C.A. No. 8224, Allen, C. (Aug. 24, 1988), slip op. at 3. *Accord In re Resorts Int'l Shareholders Litig.*, Del. Supr., 570 A.2d 259, 266 (1990); *Polk*, 507 A.2d at 535; *Friedman v. Baxter Travenol Laboratories, Inc.*, Del. Ch., C.A. No. 8209, Jacobs, V.C. (Feb. 18, 1986), slip op. at 6. Indeed, the status of this suit as a non-(b)(3) class action heightens the standard even further since this type of class action affords the members no opportunity to opt out. *See In re Amsted Industries Inc. Litig., supra*, at 1.

In exercising its business judgment and applying this heightened standard, it is not necessary for the Court to decide the merits of the case. *See Barkan v. Amsted Industries, Inc.*, Del. Supr., 567 A.2d 1279, 1284 (1989); *Rome*, 197 A.2d at 53; *In re Beatrice Companies, Inc. Litig.*, Del. Ch., C.A. No. 8248, Allen, C. (Apr. 16, 1986), slip op. at 2, *aff'd*, Del. Supr., 522 A.2d 865 (1987). How-

ever, the Court must consider a number of factors. These factors include:

> (1) The probable validity of the claims, (2) the apparent difficulties in enforcing the claims through the courts, (3) the collectibility of any judgment recovered, (4) the delay, expense, and trouble of litigation, (5) the amount of the compromise as compared with the amount and collectibility of a judgment, and (6) the views of the parties involved, pro and con.

Polk, 507 A.2d at 536. *Accord In re First Boston, Inc. Shareholders Litig.*, Del. Ch., C.A. No. 10338, Allen, C. (June 7, 1990), slip op. at 1; *In re MAXXAM Group, Inc. Stockholders Litig.*, *supra*, at 2. In this case, the parties' primary disputes rest upon factors (2) and (5): the probable validity of the claims and the amount of the compromise as compared with the probable amount of a judgment for the claims.

III. PROBABLE VALIDITY OF THE CLAIMS

At the outset, I note that the Objectors do not claim that Vitalink's Board breached its fiduciary duty of loyalty. Further, to the extent that plaintiff's initial complaint alleged a breach of the fiduciary duty of loyalty, I firmly believe that any such loyalty claim is wholly meritless. I believe that any loyalty claim is meritless because Vitalink's Board unanimously approved the transaction, because three of Vitalink's four board members were completely disinterested (and, therefore, the entire Board is deemed "disinterested", *see Aronson v. Lewis*, Del. Supr., 473 A.2d 805, 812 (1984)) and because there is no evidence that an interested party "controlled" the actions of the Board. *See generally id.*; *Roberts v. General Instrument Corp.*, Del. Ch., C.A. No. 11639, Allen, C. (Aug. 13, 1990), slip op. at 17.

A. Duty of Care

1. Duty and Standard of Review

When the Board determined to sell Vitalink, its duty of care changed from a duty to preserve the company to a duty to attain the highest price reasonably attainable for Vitalink's stockholders under the circumstances. *See Barkan*, 567 A.2d at 1286; *Mills Acquisition Co. v. Macmillan, Inc.*, Del. Supr., 559 A.2d 1261, 1288 (1989); *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, Del. Supr., 506 A.2d 173, 182 (1986). Having determined the duty of the Board, I must determine the standard I would use at trial to decide whether the Board fulfilled their duty.

> In each instance where the board is not predominantly self-interested or under the control or dominating influence of a person with a conflicting interest, the principal judicial inquiries relate to whether the board was adequately informed and acting in good faith. This court has been pointedly instructed, however, that "where issues of corporate control are at stake" action of even a disinterested board must meet an enhanced test before they will qualify for the deference that courts ordinarily accord to good faith business judgments. *See Mills Acquisition Co. v. Macmillan, Inc.*, Del. Supr., 559 A.2d 1261, 1287-88 (1989). This enhanced test requires a judicial judgment of reasonableness in the circumstances .... In such a setting, the additional level of inquiry comes to this: whether the circumstances afford a disinterested and well motivated director a basis reasonably to conclude that if the transactions contemplated by the merger agreement close, they will represent the best available alternative for the corporation and its shareholders.

Roberts, *supra*, at 17-18. Thus, the question boils down to this: did the Board have a reasonable basis to conclude that the NSC offer was the best available alternative to the corporation and its stockholders?

In this case, the Vitalink Board was considering only one offer when the members made their decision. Thus, the Board must have had a body of reliable evidence upon which to judge the adequacy of the NSC bid or must have canvassed the market to determine if it could have elicited higher bids in order to satisfy the enhanced reasonableness test described in *Roberts*. *See Barkan*, 567 A.2d at 1286-87. The Objectors claim that the Vitalink Board neither had canvassed the market to determine if it could have elicited higher bids nor had a sufficient body of reliable evidence to judge the adequacy of the bid. On the other hand, defendants argue that the Board canvassed the market and had a sufficient body of reliable evidence.

2. Canvassing the Market

From December 1990 until May 1991, Vitalink held extensive negotiations with NSC as to entering into some sort of business relationship or combination with NSC. Besides the NSC negotiations, the Board also considered whether it should conduct a public auction. However, the Board, with Kidder's advice, determined that an auction could have disastrous effects on Vitalink's competitive position. (Rein Dep. at 137-39; Valdez Dep. at 58, 173-74; Valdez Aff. ¶ 17.) The Board followed this advice even though supposedly everyone knew Vitalink was ready to make a deal. (Rein Dep. at 109.) Further, the Board considered contacting a number of technologically compatible companies but decided against it for various reasons. (See Rein Dep. at 109, 137-88; Valdez Dep. at 76.)

As stated earlier, the Board was in actual contact with A Co., B Co. and C. Co. during the spring of 1991. Ultimately, Vitalink held two meetings and a phone conversation with B Co. before B Co. indicated that it was not

interested in pursuing further negotiations regarding a business relationship or combination. (Denend Dep. at 20-21.) The Board decided not to pursue a transaction with A Co. and C Co. because they believed it would be highly complex and because they believed A Co. and C Co. had to enter into a first step transaction before Vitalink could enter the picture and, until that happened, further negotiations were meaningless. (Rein Dep. at 111-18.) Kidder advised Vitalink that it was doubtful that any other company would have an interest in pursuing a business combination transaction with Vitalink given its poor competitive position. (Valdez Aff. ¶ 22; Def. Exh. 29 at VA004257-58.)

The Objectors argue and I agree that defendants' and plaintiff's briefs contain a lot of smoke and little fire. That is, defendants and plaintiff focus on the Board's considering contacting many companies. However, when the smoke clears, the Board actually held discussions only with three entities in the context of two alternative transactions (*i.e.*, a transaction with B Co. and a three-way transaction with A Co. and C Co.) Further, I am disappointed with defendants' attempts to imply that the Board actually contacted more than these three companies when the record does not support such assertions.[1]

The Objectors also argue that the No-Shop clause, the Lockup and the termination fee prevented Vitalink from being capable of canvassing the market. Defendants argue, and I agree, that these provisions do not, in themselves,

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[1] For example, on page 35 of defendants' brief, defendants assert that Vitalink met with D Co. and refer to their brief at page 14. On page 14 in discussing Vitalink's relationship with D Co., defendants' brief refers to Rein's deposition at 143 and defendants' exhibit 24 at 4213. Both references only state that the Board considered contacting D Co. I see no authority in the record to support defendants' assertion that Vitalink held discussions with D Co. and the effort to create the impression of such discussions based on nonexistent authority is troubling to me.

prevent a company from canvassing the market. *See generally In re Fort Howard Corp. Shareholders Litigation*, Del. Ch., C.A. No. 9991, Allen, C. (Aug. 8, 1988), slip op. at 32 (where court held a lockup option and a window shopping clause did not prevent a market check), *appeal denied*, Del. Supr., 547 A.2d 633 (1988). The No-Shop agreement was subject to a fiduciary out clause whereby the Board could shop the company so as to comply with, among other things, their *Revlon* duties (*i.e.*, duty to get the highest price reasonably attainable for shareholders.) Also, the Lockup did not constitute a real impediment to an offer by a third party. (*See* Valdez Dep. at 137.) Finally, the parties ultimately agreed to limit the termination fee to $2,771,331. This amount represented $1 per share for each of the Lockup option shares. If this amount is spread across 100% of Vitalink's shares, it represents $.199 per share or a little less than 1.9% of the value of the transaction. I do not believe this possible payment prevented a canvass of the market. *See generally Roberts*, *supra*, at 21 (where the Court held that a 2% breakup fee was limited); *Braunschweiger v. American Home Shield Corp.*, Del. Ch., C.A. No. 10755, Allen, C. (Oct. 26, 1989), slip op. at 19 (where the Court held that a $.25 per share cancellation fee was not onerous).

Ultimately, in determining whether the Board canvassed the market, I have considered a number of factors. First, Vitalink held discussions with three companies besides NSC in the context of two transactions alternative to the NSC transaction. Although these discussions gave an indication as to the extent of the market's interest with Vitalink at any price, the discussions gave little indication as to the adequacy of the NSC bid because negotiations with these companies broke off before the parties ever discussed valuation issues. (Denend Dep. at 26-27.) Second, the discussions were somewhat contemporaneous with the NSC agreement. That is, the discussions with these three companies concluded by mid-March 1991 and were sufficiently

close to the May agreement so that the timing of the discussions, in itself, did not jeopardize whatever information the discussions provided as to the adequacy of the NSC bid. Third, the Lockup option, the No-Shop clause and termination fees did not prevent, in themselves, a canvass of the market. Finally, forty-five days passed between the public announcement of the transaction and the closing of the tender offer. In this period, no bidder came forward.

The goal of the canvassing requirement is to ensure that a board has adequately informed itself as to whether it is getting the best deal reasonably possible for the shareholders. After considering the factors enumerated earlier, I am persuaded that the actions of the Board were not an effective probe of the market and did not provide the Board sufficient information to judge the adequacy of the NSC bid. The Board's actual contacts with other companies only indicated that some members of the market were unable or unwilling to enter into a transaction with Vitalink at any price. Further, I refuse to rely principally upon the market test as constituting a canvass of the market for two reasons. First, I refuse to rely on it because the term canvass connotes greater action by the Board than an implicit market test. Second, I refuse to rely principally on the implicit market test as constituting a canvass of the market because of my heavy reliance on this factor in deciding that the Board had a sufficient body of reliable evidence to judge the adequacy of the NSC bid. That is, if I also rely on it here, it will be difficult to distinguish between the two tests. Thus, I hold that the actions of the Board did not constitute a canvass of the market.

3. Body of Reliable Evidence

With respect to the issue whether the Board had a sufficient body of reliable evidence upon which to judge the adequacy of NSC's bid, the first element the Board relied

upon was the Kidder fairness opinion as to the proposed transaction with NSC. In deciding that the transaction would be fair to Vitalink, Kidder performed three types of valuation analyses: a discounted cash flow analysis, a comparable transaction analysis and a comparable company analysis.

The Delaware courts have affirmed the validity of the discounted cash flow method of valuation repeatedly. *See Cede & Co. v. Technicolor*, Del. Ch., C.A. No. 7129, Allen, C. (Oct. 19, 1990), slip op. at 17; *Neal v. Alabama By-Products Corp.*, Del Ch., C.A. No. 8282, Chandler, V.C. (Aug. 1, 1990), slip op. at 21, *aff'd*, Del. Supr., 588 A.2d 255 (1991).

> The DCF model entails three basic components: an estimation of net cash flows that the firm will generate and when, over some period; a terminal or residual value equal to the future value, as of the end of the projection period; and finally a cost of capital with which to discount to a present value both the projected net cash flows and the estimated terminal or residual value.

Cede & Co., supra, at 17-18.

In this case, Kidder's discounted cash flow analysis valued Vitalink between $9.50 and $11.75 per share. In evaluating a discounted cash flow analysis, the quality of the projections relied upon is central to the reliability of the underlying methodology. *See Harris v. Rapid-American Corp.*, Del. Ch., C.A. No. 6462, Chandler, V.C. (Oct. 2, 1990), slip op. at 15. In preparing their analysis, Kidder relied upon information that was overly optimistic: the projected revenue growth was dependent on new product development that was no longer on schedule. (*See* Objectors' Exh. B at 6.)

The Objectors attack Kidder's discounted cash flow analysis because of its reliance on these overly optimistic pro-

jections. This attack is completely meritless. The use of the overly optimistic projections, if anything, overvalues Vitalink. Thus, since NSC's bid rests within the value range even using the overly optimistic projections, the use of this methodology is a very strong indication as to the adequacy of the NSC bid.

The Objectors also attack Kidder's discounted cash flow analysis by contending that Kidder manipulated the discount rate and the terminal multiple it used. That is, Kidder used a 14% discount rate and terminal multiples of 10, 12 and 14 in its April 1990 analysis. In its June 1990 analysis, Kidder again used a 14% discount rate and terminal multiples of 14. (Valdez Dep. Exh 2 at KP001884.) However, Kidder used terminal multiples ranging from 3-6 and discount rates from 18-22% in its May 1991 analysis. (Valdez Dep. Exh. 10 at KP000048.)

The Objectors take issue not so much with the correctness of these numbers but with the failure of the Board to question Kidder's changes. The defendants and plaintiff contend, and I agree, that the changes Kidder made were appropriate. Vitalink was a very different company in May 1991 than it was in February and April 1990. "In February of 1990 the company was growing, the company still had market share, which would be termed significant. In March 1991 the company's revenues were declining. The company's market share within the broader context of the industry was also declining." (Valdez Dep. at 19-20.) Vitalink was a much riskier company in May 1991 than in February and April 1990. (*Id.*) Thus, Kidder's adjustments to account for these differences were appropriate.

The failure of Vitalink's Board to question Kidder regarding the changes is irrelevant. At this juncture, the issue only is whether the Board had reliable information upon which to judge whether the NSC bid was the best offer reasonably attainable. The failure to inquire as to why Kidder made the adjustments makes no difference

because, in fact, the adjustments were appropriate and the discounted cash flow analysis constituted reliable information. Further, in all likelihood, the Board thought, as I do, that the reason for the changes was obvious: the severe downturn in Vitalink's prospects.

The second valuation method Kidder used in determining the fairness of the transaction was the comparable transaction method. This method identifies transactions comparable with the one at hand and adjusts the value of those transactions to account for the differences between the companies in the prior transactions and the companies in the pending transaction.

In this case, Kidder's comparable transactions analysis valued Vitalink between $12.27 and $21.02 per share. However, Kidder downplayed the reliability of this methodology because it relied on transactions from the late 1980s where values were high and financing was readily available and because it relied on transactions for growing companies as opposed to companies like Vitalink that were declining. (Objectors' Exh. B. at 6.)

The differences in the economic condition of the takeover market between the late 1980s and present are obvious. Thus, reliance on transactions from that era clearly overvalue the Vitalink transaction. The question then becomes to what extent did the comparable transactions analysis overvalue the Vitalink transaction. However, Kidder did not indicate nor did the Board inquire as to the extent of the method's overvaluation.

The failure of the Board to inquire and of Kidder to determine the extent of the overvaluation undermines defendants' argument that the Board had sufficiently reliable information to determine the adequacy of NSC's bid. The Board or, in its stead, Kidder should have accounted fully for the bid's seeming inadequacy under this analysis. Without this inquiry, a cloud of doubt as to the adequacy

of NSC's bid remained on Kidder's analysis. The Board should have *fully* accounted for this cloud.

The final valuation method that Kidder used was the comparable company analysis. This Court has affirmed the general validity of this approach repeatedly. *See Harris, supra*, at 21. This method first identifies comparable publicly traded companies. *See id.* at 19-20. It then calculates the value of the company to be valued through the application of earnings and other multiples to the comparable companies and the company to be valued. *See id.*

Under the comparable company method, Kidder determined Vitalink's value to be between $7.14 and $11.49 per share. The Objectors first attack Kidder's comparable company analysis by pointing out that Salomon Brothers ("Salomon"), NSC's investment banker, failed to use this method in valuing Vitalink. However, the mere non-use by Salomon of this method is irrelevant. As noted earlier, the Delaware courts have affirmed the validity of this approach repeatedly. The failure of one investment banker to use the methodology, in itself, is not an indication that it was an unreliable method of valuing the pending transaction.

The Objectors next contend that Kidder's comparable company valuation is flawed because it excluded four "upper tier" companies from its analysis and, yet, included the lower than "lower tier" companies. (*See* Valdez Exh. 10 at KP000064.) Defendants argue and I agree that the exclusion of the upper tier companies by Kidder was appropriate. Obviously, the utility of a comparable company approach depends on the similarity between the company the court is valuing and the companies used for comparison. *See Neal v. Alabama By-Products Corp.*, Del. Ch., C.A. No. 8282, Chandler, V.C. (Aug. 1, 1990), slip op. at 21 n.6, *aff'd*, Del. Supr., 588 A.2d 255 (1991); *Citron v. E.I. DuPont de Nemours & Co.*, Del. Ch., 584 A.2d 490, 510 (1990). The exclusion of noncomparable companies makes this type of valuation analysis more reliable. In this

case, Vitalink clearly had become a lower tier company. Vitalink's revenues and earnings were falling quickly in late 1990 and early 1991. Further, despite Vitalink's strong customer base, its outlook was bleak. (Def. Exh. 17 at KP001708; Rein Dep. at 104.) The exclusion of the upper tier companies from its analysis made Kidder's analysis more reliable.

The Objectors contend that if Kidder properly excluded upper tier companies, it also should have excluded companies they allege to be lower than the lower tier companies. The Objectors argue that these lower than the lower tier companies were noncomparable with Vitalink because of the differences in income. (*See* Objectors' Brief at 24.) However, income is not the only factor that determines the comparability of companies. A court can consider many factors in determining the comparability of companies. Such factors include product mix, revenue, revenue and earnings growth rates, assets and geographic markets. The Objectors do not attempt to distinguish Vitalink from the lower than the lower tier companies on the basis of any factor except income. In my opinion, given the Objectors' ability to cite only differences in income and given Vitalink's bleak outlook, Kidder's inclusion of all of the lower tier companies and not the upper tier companies was appropriate.

Kidder used these three valuation methods (*i.e.*, the discounted cash flow analysis, comparable transactions analysis and comparable company analysis) as the primary basis for opining that the proposed transaction with NSC was fair to Vitalink. Despite the infirmities of its comparable transaction valuation, overall, I believe that Kidder's fairness opinion constituted reliable information upon which the Board partially could judge the adequacy of NSC's offer.

Besides Kidder's fairness opinion the Board relied on a number of other factors in deciding that NSC's bid was

the best bid available. Before accepting NSC's third bid, the Board rejected two offers it thought were inadequate. Additionally, NSC conditioned its offer on the granting of the Lockup. (Def. Exh. 28 at VA004253; Altman Dep. at 44.) NSC also conditioned its offer on the execution of the Control Agreements. (Altman Dep. at 30-32.) Moreover, the Board believed that NSC's final offer was "about as close to a turned-inside-out-pocket offer [as Vitalink was] going to get." (Rein Dep. at 186.) Further, the bid represented approximately a 23.5% premium over market price. Also, Kidder's preliminary analysis indicated that $10 per share represented a good price. (Valdez Dep. 124-126; Valdez Aff. ¶ 21.) Further, Vitalink had constructed Kidder's fee arrangement so that Kidder would be paid more if a third party (*i.e.*, not NSC) consummated the merger with Vitalink. Thus, Kidder's failure to get such a third party to consummate the merger is, in itself, an indication that no other bidder would have paid more than $10.50 per share. Similarly, the final factor upon which the Board relied in determining the adequacy of NSC's bid was a market test administered by the circumstances. "[W]hen it is widely known that some change of control is in the offing and no rival bids are forthcoming over an extended period of time, that fact is supportive of the board's decision to proceed." *Barkan*, 567 A.2d at 1287. In this case, forty-five days passed between the time the parties first publicly announced the transaction (May 6, 1991) and the closing of the tender offer (June 20, 1991) without even an inquiry from an interested acquiror. (Valdez Aff. ¶ 34.)

The Objectors contend that the Board's reliance on this last factor, the implicit market test, is meritless. They argue that no potential bidder came forward because of NSC's Lockup and because of the No-Shop clause. However, Valdez testified that the Lockup "was not an insurmountable barrier for another alternative buyer to slip forward." (Valdez Dep. at 137.) Also, the No-Shop clause

was subject to a fiduciary out clause. (Rein Exh. 2 at 10.) I agree with defendants' arguments that the Lockup option and the No-Shop clause were, at best, minimal impediments to an implicit market test.

In making its argument that the Board did not have a sufficient body of reliable evidence upon which to judge the adequacy of NSC's bid, the Objectors also argue that the Board breached their duty of care by failing to determine the inherent value of Vitalink before accepting the NSC offer. The Objectors contend that this ignorance resulted in the Board not having an adequate basis to determine whether NSC's bid was the best offer reasonably possible. *See generally In re Trans World Airlines, Inc. Shareholders Litig.*, C.A. No. 9844, Allen, C. (Oct. 21, 1988), slip op. at 11, 18.

In *TWA*, the special committee basically did not know that its duty was to attain the best offer reasonably possible. *See id.* at 8-9. Further, to the extent the special committee did know they had such a duty, they thought its financial advisor would fulfill it. *Id.* at 10. However, the financial advisor believed its duty was only to address the issue of the offer's fairness. *Id.* Finally, in deciding whether the offer was fair, the financial advisor relied on a number of valuation techniques that resulted in a broad range of values ($14.50 to $66.29 per share) without expressing to the committee how it used the different valuation results in concluding that the offer was fair. *Id.* at 11.

The focus of the *TWA* decision was not so much whether the special committee knew the company's inherent value per se but whether the special committee had sufficient information to satisfy its duty to attain the highest price reasonably possible for the shareholders. I realize that the Vitalink Board did not have perfect information. Nevertheless, I hold that the Vitalink Board had sufficient information so as to satisfy the concerns of the Court in

TWA. Further, although the circumstances in which a body of reliable evidence exists is limited, *see Barkan*, 567 A.2d at 1287, I hold that this same information constituted a body of reliable evidence upon which the Vitalink Board could judge the adequacy of NSC's bid.

This body of information which I hold as sufficient to satisfy *TWA* and as constituting a body of reliable evidence consists of a number of elements. First, the parties negotiated for a number of months over the terms and structure of their relationship. Second, the Board rejected two bids before accepting NSC's third offer. Third, the Board believed that this was NSC's best offer. (Rein Dep. at 186.) Indeed, NSC conditioned its offer on the granting of the Lockup. (Def. Exh. 28 at VA004253; Altman Dep. at 44.) Also NSC conditioned its offer on the execution of the Control Agreements. (Altman Dep. at 30-32.) Fourth, the offer represented approximately a 23.5% premium over Vitalink's trading price. Fifth, Vitalink structured Kidder's fee agreement so that it had an incentive for Vitalink to consummate the transaction at the highest possible price. (*See* Def. Exh. 31 at KP000576.) These five elements afforded a reasonable basis for the Board to conclude that it was getting NSC's best bid.

In holding that the Board had a reasonable basis to conclude that NSC's last offer was the best overall offer, I rely on a number of other factors besides the factors enumerated above. First, Kidder produced a range of Vitalink's fair values ($7.14 to $21.02 per share). This range was much more limited than the range presented to the special committee in *TWA*. Second, Kidder's preliminary analysis indicated that a $10 per share price was a good price. (*See* Valdez Dep. at 124-27; Valdez Aff. ¶ 21.) Third, Kidder opined that the $10.50 price was fair. Fourth, the Vitalink Board and Kidder believed no other bidder was interested. Fifth, Vitalink structured its fee agreement with Kidder so that Kidder had an incentive to have Vitalink consummate a sale with a third party. Finally, and most

importantly, no third party even inquired as to making a competing bid.

Ultimately, I believe that all of these factors combine to allay the Court's concerns in *TWA* over whether a board sufficiently knows its duty and has a sufficient basis to conclude that it has satisfied its duty. Correspondingly, I find that these factors constituted a body of reliable evidence such that the Vitalink Board could reasonably conclude that it was getting the best deal possible for Vitalink's shareholders. Thus, I conclude that the Vitalink Board satisfied its duty of care by having reliable grounds upon which to judge the adequacy of NSC's offer.

B. Duty of Candor

The Objectors argue that the Board failed to satisfy their duty of candor under Delaware law and their duty not to make material misrepresentations in the offering documents under federal law. In making these assertions, the Objectors first contend that the Offer to Purchase and the Schedule 14D-9 did not discuss or summarize Kidder's valuation analysis and its limitations nor did they contain a summary of the various valuation ranges that Kidder calculated. The Objectors argue that defendants' subsequent inclusion of such information in the Notice of Merger was an implicit admission as to the information's materiality. The Objectors' second contention is that the Board violated its disclosure duties by failing to inform the stockholders that they were not soliciting bids from third parties. Finally, the Objectors take issue with the deletion of the sentence: "[w]e have not been represented to, and did not solicit third party indications of interest in acquiring all or any part of the Company." (Objectors' Exh. D at KP000571.) The Objectors argue that the deletion of this sentence from the Kidder opinion that Vitalink sent to its shareholders was inappropriate.

Defendants and plaintiff argue that the Objectors' contentions as to the failure to fully disclose Kidder's opinion

are meritless. Defendants contend that Kidder advised the Board that the range of fair values produced by the comparable transaction analysis was overstated. Defendants argue that the analysis was misleading because it overstated Vitalink's value. Thus, defendants argue it was not material. Similarly, the Board concluded that Kidder's discounted cash flow analysis produced an overly optimistic result because Kidder based its analysis on product development that was behind schedule. Defendants argue that the analysis was misleading because it overstated Vitalink's value. Thus, defendants argue it was not material. Finally, defendants argue that the Board concluded that Kidder's comparable company analysis produced a result that only confirmed the Board's and Kidder's opinions and would not have changed the total mix of information sent to the shareholders had it been disclosed. Thus, defendants argue, it was not material.

Plaintiff and defendants failed to address the Objectors' second disclosure argument. However, defendants argue that the Objectors' third argument regarding the deletion of the sentence in the Kidder opinion is meritless. Defendants argue that they deleted the sentence in order to remove any suggestion that Kidder did not concur with the Board's decision not to pursue offers from third parties while negotiating with NSC. Defendants argue that the deletion was not misleading.

Before I address the specific arguments, I first must discuss the disclosure standards. Materiality exists when:

> the omitted fact would have assumed actual significance in the deliberations of the reasonable shareholder. Put another way there must be a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the total mix of information available.

Rosenblatt v. Getty Oil Co., Del. Supr., 493 A.2d 929, 944 1985) (quoting *TSC Industries Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976)). An entity need not disclose a financial advisor's underlying facts and analyses in every case. *See In re Dataproducts Corp. Shareholders Litig.*, Del. Ch., C.A. No. 11164, Jacobs, V.C. (Aug. 22, 1991), slip op. at 16-17. In deciding whether a court should require disclosure of this type of information, a court should weigh the potential benefits of the disclosure against its potential harm. *See Weinberger v. Rio Grande Industries Inc.*, Del. Ch., 519 A.2d 116, 126-27 (1986). Further, "[t]o be the subject of a disclosure obligation, information relating to value must be considered reliable." *Van de Walle v. Unimation, Inc.*, Del. Ch., C.A. No. 7046, Jacobs, V.C. (Mar. 6, 1991), slip op. at 37.

At the outset, I note that I do not agree with the Objectors' assertion that the subsequent disclosure of the underlying details of the Kidder opinion in the Notice of Merger acted as an implicit admission of its materiality. There are many possible reasons why the disclosure was only included in the later disclosure (*e.g.*, the Board may have not believed it was material but was overly cautious as to what disclosures to make after it had some time to think about this lawsuit). The Objectors have failed to persuade me that the subsequent disclosure was made because the Board believed it was material.

As to the Objectors' arguments regarding defendants failure to disclose Kidder's valuation techniques, analyses and limitations, I agree with defendants that the nondisclosure of Kidder's discounted cash flow analysis and range of value ($9.50 to $11.75 per share) was proper. The nondisclosure was proper because the analysis was not material. The analysis was not material because its potential benefit was, at best, minimal: to act as a mere affirmance to the shareholders of the Board's message that this was a very good deal. However, its potential harm was great. Even if the disclosure included a sentence explaining why

the analysis was overly optimistic, it could have misled shareholders into believing that a higher price was attainable. That is, because the Board did not know the extent of the overstatement and, therefore, could not have disclosed the extent of the overstatement, the shareholders could have read the disclosure and reasonably believed that even if $11.75 was not attainable, a price higher than $10.50 was reasonably attainable when all of the circumstances indicated that this was not the case. Since I believe the potential harm of the disclosure of this analysis outweighs its potential benefit, the Board did not have to disclose it. *See Weinberger*, 519 A.2d at 126-29.

I also agree with defendants that disclosure of Kidder's comparable transaction analysis would have been inappropriate. Clearly, the analysis produced an unreliable range of values ($12.27 to $21.02 per share) because Kidder based its analysis on market conditions that have changed drastically. Disclosure of this analysis would have presented an enormous potential for harm to the shareholders. Even if the disclosure included a sentence why Kidder believed the analysis produced an inflated range, it could have mislead shareholders into believing that a higher price was attainable. That is, because the Board did not know the extent by which the range was inflated and, therefore, could not have disclosed it, the shareholders could have read the disclosure and reasonably believed that even if $21.02 per share was not attainable, a price higher than $10.50 per share was reasonably attainable when all of the circumstances indicated that this was not the case. Further, Kidder gave little or no weight to this analysis in its opinion. (*See* Valdez Aff. ¶ 25.) Thus, it was proper for the Board to not disclose this analysis. *See generally Van de Walle, supra*, at 37 (where court held that unreliable information cannot be the object of a disclosure obligation); *In re Genentech, Inc. Shareholders Litig.*, Del. Ch., C.A. No. 11377, Chandler, V.C. (June 6, 1990), slip op. at 19 (where court relied, in part, on the fact that the investment banker did

not give any serious consideration to certain valuation ranges in determining that the company did not have to disclose them); *Weinberger*, 519 A.2d at 527-30 (where court held that the potential benefits of a disclosure must be weighed against its potential harm and where court relied, in part, on the fact that the investment banker gave little or no weight to a valuation analysis in determining that it was unreliable and did not have to be disclosed.)

I also agree with defendants' claim that the disclosure of the comparable company range of fair value ($7.14 to $11.49 per share) was not necessary. I am not persuaded that disclosure of this analysis would have changed the total mix of information received by the shareholders. Also, it is necessary to draw a line somewhere or else disclosures will become so voluminous that they no longer serve their purpose. *See TCG Securities, Inc. v. Southern Union Co.*, Del. Ch., C.A. No. 11282, Chandler, V.C. (Jan. 31, 1990), slip op. at 18. Thus, I hold that the comparable company analysis falls outside of this line of materiality.

As to the Objectors' second disclosure argument that the Board should have disclosed that it did not canvass the market, I hold that this disclosure was not necessary. The reason for the canvassing requirement is to ensure that a board is getting the best deal possible for the shareholders. *See Barkan*, 567 A.2d at 1287. However, a court can also be so ensured when a board has a reliable body of evidence with which to evaluate the fairness of a transaction. *See id.* I have held earlier that, even though the Vitalink Board did not canvass the market, the Board did have such a body of reliable evidence. Thus, the Board has proven that it has satisfied its duty to get the best deal reasonably possible for the shareholders. It is irrelevant by which route (*i.e.*, the canvass route or the body of reliable evidence route) the Board proved that it satisfied its duty. Therefore, I hold that the Board's non-

canvassing was immaterial and did not have to be disclosed.

As to the Objectors' third contention that the deletion of the sentence from the Kidder opinion sent to shareholders was inappropriate, I agree with defendants that the deletion was not improper. The deletion helps to remove any suggestion that Kidder did not agree with the Board's decision not to pursue third party offers. Further, the edited version of the opinion does not suggest or imply in any way that Kidder was requested to solicit third party offers. Thus, the deletion of the sentence was not misleading and, therefore, not improper.

C. Aiding and Abetting Claims Against NSC

Plaintiff's original complaint included claims against NSC for aiding and abetting the alleged wrongdoings of the Vitalink Board. The Objectors do not contend nor is there any evidence that these claims are meritorious.

IV. WEIGHING THE VALUE OF THE SETTLEMENT AGREEMENT AGAINST THE VALUE OF THE CLAIMS

The second major facet of the parties' arguments deals with the value of the Settlement Agreement as compared to the value of the claims. The Settlement Agreement between plaintiff and defendants called for: (1) NSC to extend the tender offer for ten days until June 20, 1991; (2) NSC and defendants to amend the cancellation agreement under the Lockup so as to limit the cancellation amount payable to NSC to $2,771,331 ($1 per share for each Lockup share); (3) NSC and defendants to amend the merger agreement so as to limit Vitalink's reimbursement of NSC fees and expenses to $1,750,000; and (4) NSC and defendants to publicly announce the agreements stated in (1)-(3).

The Objectors argue that the purported benefits conveyed by the Settlement Agreement are wholly illusory.

They argue that the extension of the tender offer conveyed no benefit because there was no expectation that a third party offer would arise and because the Lockup option and the No-Shop acted as a severe impediment to such offers. They also argue that the amendments to the Lockup option and termination agreements were illusory because the Lockup and the No-Shop acted as a severe impediment to the amendments ever becoming operative. Further, assuming that the Lockup and No-Shop did not act as an impediment to third party offers, the Objectors argue that the amendments to the cancellation amount payable and reimbursement agreement were illusory because any potential third party offer would have come forward already and made his bid. Also, the limitations on these amendments, they argue, were illusory in themselves because the parties did not know whether they would be exceeded if they became payable.

The extension acted to enhance Vitalink's market check and to add to the Board's body of reliable evidence that this was the best deal reasonably attainable for the shareholders. As discussed earlier, the Lockup option and No-Shop acted as no real impediment to third party offers. Thus, the extension of the tender offer provided some benefit to Vitalink's shareholders.

As far as the amendments to the cancellation agreement and reimbursement agreement, the Lockup and No-Shop acted as no real impediment to a third party offer. Thus, the amendments could have become operative. Further, the amendments were not illusory because the parties did not expect a third party offer to arise. That is, just because the parties did not expect a third party offer did not mean that one could not arise. Finally, just because the parties did not know whether the limitation amounts would be exceeded does not mean they could not have been exceeded. Indeed, if NSC expended more than $1,750,000 on its expenses and required more than $2,771,331 for its Lockup cancellation, it would not have been unusual. Since the extension of the tender offer period provided an enhanced market check and the amendments to the Lockup cancellation agreement and reimbursement agreement pro-

vided certainty that the total expenses of cancellation would not exceed a certain amount, the settlement provided some, albeit speculative, value to Vitalink shareholders and did not convey only illusory benefits.

The Objectors argue that the value of the settlement is minimal in comparison with the claims asserted and the claims that could be asserted. As far as the claims that could be asserted, there is no indication of their merit. As far as the claims asserted, I have found them to be very weak. Thus, I hold that the benefits conferred by the settlement, even though they are speculative, are of sufficient value for the claims covered by the Settlement Agreement.

The Objectors also argue that the record is insufficiently developed to allow me to evaluate the proposed settlement in an informed manner. *See generally In re Republic American Corp. Litigation*, Del. Ch., C.A. No. 10112, Allen, C. (June 7, 1990), slip op. at 2 (where court declined to approve or reject a settlement proposal because the record contained insufficient information). I disagree with the Objectors. I have found the record to be sufficiently developed so as to afford a reasonable basis to respond to all of the asserted claims. Since I hold that there is an adequate basis upon which I am able to determine whether the Settlement Agreement was fair and since I have found the Settlement Agreement to be fair and reasonable, I approve the Settlement Agreement.

V. PLAINTIFF'S ATTORNEYS' FEES AND EXPENSES

Plaintiff requests me to award $275,000 for its attorneys' fees and expenses. In a class action, a court should award reasonable plaintiff's attorneys' fees and expenses where the attorneys achieve benefits for the class. *See Chrysler Corp. v. Dann*, Del. Supr., 223 A.2d 384, 386 (1966). In determining the issue of the amount of fee allowances in stockholder actions, a court should consider: (1) the benefits achieved in the action; (2) whether the fee is contin-

gent; (3) the efforts of counsel; (4) the difficulty of the litigation; and (5) the standing and ability of counsel involved. *See e.g., Sugarland Industries, Inc. v. Thomas*, Del. Supr., 420 A.2d 142, 142-50 (1980). Specifically, in evaluating fee requests where the settlement does not create a settlement fund, a court must apply a three-pronged test in evaluating the propriety of a fee request: (1) whether the claims were meritorious when plaintiff filed them; (2) whether the settlement creates a benefit to the corporatiton; and 93) whether plaintiff's litigation was causally related to the benefits. *See Allied Artists Pictures Corp.*, 413 A.2d at 878-80.

A claim is meritorious if there is some reasonable hope for its success when plaintiff filed it. *See Chrysler Corp.*, 223 A.2d at 384. The litigation is causally related to the benefit if the benefit arises after plaintiff filed the lawsuit and the defendant corporation is unable to demonstrate "that the lawsuit did not in any way cause their action." *Allied Artists Pictures Corp.*, 413 A.2d at 880.

Plaintiff argues and I agree that plaintiff's claims were meritorious when it filed them. Plaintiff reasonably believed that the claim had a good chance of success because Denend acted as negotiator for the transaction while also agreeing to work for Vitalink if NSC acquired it and because the Board had not contacted many other companies before agreeing to the transaction.

As far as the second factor, the benefits achieved from the litigation generally constitute the factor given the greatest weight in determining the fee to be awarded. *See In re Anderson Clayton Stockholders' Litig.*, Del. Ch., C.A. No. 8387, Allen, C. (Apr. 14, 1988), slip op. at 3. In this case, the settlement called for an extension of the tender offer for ten days. This extension provided an enhanced market check. Also, the settlement called for a limitation on the amount of the reimbursement agreement and the Lockup cancellation agreement. These limitations gave po-

tential third parties greater certainty as to how much a successful bid for Vitalink would cost. Further, the settlement called for the public announcement of these agreement. This public announcement further enhanced the market check afforded by the extension of the tender offer and the limitation of reimbursement agreement and Lockup termination agreement. Ultimately, the settlement provided speculative benefits to the class. Nonetheless, the class benefitted.

As to the third factor, there is a presumption of a causal relationship between the plaintiff's efforts and the benefits. *See In re Beatrice Companies, Inc. Litig., supra*, at 18. However, this presumption is not even necessary in this case because all agree that the benefits from the settlement were a direct result of the litigation.

Since plaintiff's attorneys have met all three prongs, I believe they are entitled to attorneys' fees. In evaluating the amount of the fee request, plaintiff relies on the contingent nature of the fee, the quality of legal services, the standing and ability of counsel and public policy considerations in arguing that I should award the entire $275,000.

Plaintiff's attorneys took this case on a contingent basis. In all fairness, the contingent nature of its fee agreement demands a higher fee for its work. *See Joseph v. Shell Oil Co.*, Del. Ch., C.A. No. 7450, Hartnett, V.C. (Apr. 19, 1985), slip op. at 14, *aff'd per curiam, Selfe v. Joseph*, Del. Supr., 501 A.2d 409 (1985).

The Objectors contend that plaintiff's attorneys failed to respond to some of its questions as to the proposed settlement. (Objectors' Brief at 39 fn. 15.) However, I believe that plaintiff's attorneys adequately responded to this claim at the settlement hearing. (*See* Squitieri at 75-76.) Thus, there is nothing that can lead me to believe that plaintiff's attorneys' services were anything but expeditious and effective.

As to plaintiff's attorneys' standing and ability, I find them to be in good standing and highly experienced in shareholder class action suits. "Lastly, I am mindful of the significant institutional role of class and derivative actions in the enforcement of the fiduciary duties assumed by corporate officers and directors." *In re Anderson Clayton Stockholders' Litig.*, *supra*, at 13.

After evaluating the contingent nature of the fee, the quality of legal services, the standing and ability of counsel, and the public policy considerations, I find $275,000 to be reasonable and award plaintiff's attorneys this amount.

VI. CONCLUSION

I find that the shareholders' due care and candor claims carry very little chance of success at trial. Further, I find that the Settlement Agreement conveyed some benefit to the shareholders. Thus, I hold that the Settlement Agreement is fair and approve it. Finally, I award $275,000 to plaintiff's attorneys for their fee and expenses.

An Order consistent with this opinion shall be prepared and submitted by counsel for the plaintiff and defendants.

APPENDIX D

Order and Final Judgment of the Court of Chancery of Delaware Approving Settlement

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE IN AND FOR NEW CASTLE COUNTY

CONSOLIDATED C.A. No. 12085

IN RE VITALINK COMMUNICATIONS CORPORATION SHAREHOLDERS LITIGATION

ORDER AND FINAL JUDGMENT

AND NOW, this 15th day of November, 1991, the proposed settlement of this consolidated action (the "Consolidated Action") having come on to be heard on September 16, 1991, pursuant to the Order entered herein on July 18, 1991 (the "Order") and the Stipulation and Agreement of Compromise, Settlement and Release dated June 10, 1991 (the "Stipulation" or the "Settlement"); and the Court having determined that notice of said hearing was given in accordance with the Order to members of the class as certified by the Court in the Order (the "Class") and that said notice was the best notice practicable and constitutes due and sufficient notice; and the parties having appeared in person and/or by their attorneys of record; and the said person and/or attorneys for the respective parties having been heard in support of the Settlement of the Consolidated Action; and an opportunity to be heard having been given to all other persons desiring to be heard; and the entire matter of the Settlement having been considered by the Court;

IT IS ORDERED, ADJUDGED AND DECREED as follows:

1. The Notice of Pendency of Class Action, Class Action Determination, Proposed Settlement, Settlement Hearing and Right to Appear (the "Notice to the Class") has been

given to the members of the Class pursuant to and in the manner directed by this Court's Order of July 18, 1991; proof of mailing of said notice was filed with the Court by counsel for Vitalink Communications Corporation ("Vitalink") at or before the hearing; and full opportunity to be heard has been offered to all parties, Class members and persons in interest.

2. The Settlement is found to be fair, reasonable, adequate and in the best interests of the plaintiffs and other members of the Class and is hereby approved. The parties to the Stipulation are hereby authorized and directed to comply with and consummate the Settlement in accordance with its terms and provisions.

3. This Order and Final Judgment shall not constitute any evidence or admission by any party herein that any acts of wrongdoing have been committed by any of the parties to this Consolidated Action and shall not be deemed to create any inference that there is any liability therefor.

4. The Consolidated Action is hereby dismissed on the merits with prejudice as to all the defendants and the Defendants' Affiliates (as defined below) and against the plaintiffs and all other members of the Class without costs, except as provided in the Stipulation. All claims, rights, causes of action, suits, matters and issues, known or unknown, that arise now or hereafter out of, or that relate to, or that are, were or could have been asserted in connection with, Vitalink's and Network Systems Corporation's ("NSC") employment agreements, change of control agreements, stock arrangements, and similar arrangements with Vitalink's employees, the Stock Option Agreement, NSC's proposals to acquire Vitalink stock (including, without limitation, the Offer, the Merger Agreement and the Merger), the disclosures made in the Schedule 14D-9, the Offer and the Merger, or any matters, transactions or occurrences referred to in the complaints, or any other complaint in the Consolidated Action, or in the California

Actions (as defined in paragraph 6 of the Stipulation), or any public statements, announcements or other activities relating to any of the foregoing, or the Settlement (except for an action to enforce compliance with the terms of the Settlement or an action for appraisal rights under Sections 253(d) and 262 of the Delaware General Corporation Law) (the "Settled Claims"), by any member of the Class or by Vitalink, either directly, individually, derivatively, representatively or in any other capacity against any of the defendants in the Consolidated Action or the California Actions, their respective present or former officers, directors, stockholders, agents, employees, attorneys, representatives, advisors, investment bankers (including, without limitation, Kidder, Peabody & Co. and Salomon Brothers Inc. and their officers, directors, agents and employees), commercial bankers, accountants, insurers, trustees, parents, affiliates, subsidiaries (direct or indirect, including, without limitation, NSC Acquisition Corp.), directors and officers of such parents, affiliates and subsidiaries, general and limited partners, heirs, executors, personal representatives, estates, administrators, successors and assigns (collectively, the "Defendants' Affiliates"), are hereby compromised, settled, released and discharged.

5. The plaintiffs' attorneys are hereby awarded fees of $275,000, which fees and expenses the Court finds to be fair and reasonable and which Vitalink shall pay to the plaintiffs' attorneys in accordance with the terms of the Stipulation.

6. Without affecting the finality of this Order and Final Judgment in any way, the Court hereby reserves jurisdiction for the purpose of taking any action that may be appropriate to give effect to or enforce this Order and Final Judgment.

William B. Chandler, III
Vice Chancellor

APPENDIX E

The Judgment (Mandate) Sought To Be Reviewed

MANDATE

THE SUPREME COURT OF THE STATE OF DELAWARE

C.A. No. 12085

To Court of Chancery of the State of Delaware in and for New Castle County:

Greetings:

WHEREAS, in the case of:

John P. McCarthy Profit Sharing Plan and Vitalink, et al. v. Charles L. Grimes, et al.

a certain judgment or order was entered on the 15th day of November 1991, to which reference is hereby made; and

WHEREAS, by appropriate proceedings the judgment or order was duly appealed to this Court, and after consideration has been finally determined, as appears from the opinion or order of this Court filed on April 30, 1992, a certified copy of which is attached hereto;

ON CONSIDERATION WHEREOF IT IS ORDERED AND ADJUDGED that the judgment or order be and it is hereby affirmed.

SIGNED, SEALED AND
ATTESTED BY:

Margaret Lyle
Clerk of the Supreme Court

Issued May 19, 1992

Supreme Court No. 468, 1991

APPENDIX F

Excerpt from U.S. Const. Amendment 14

No state . . . shall deprive any person of . . . property, without due process of law . . . .

APPENDIX G

Rules of the Court of Chancery of Delaware, Rule 23

RULE 23. CLASS ACTIONS

(a) Requisites to Class Action. One or more members of a class may sue or be sued as representative parties on behalf of all only if (1) the class is so numerous that joinder of all members is impracticable, (2) there are questions of law or fact common to the class, (3) the claims or defenses of the representative parties are typical of the claims or defenses of the class, and (4) the representative parties will fairly and adequately protect the interests of the class.

(b) Class Actions Maintainable. An action may be maintained as a class action if the prerequisites of paragraph (a) are satisfied, and in addition:

(1) The prosecution of separate actions by or against individual members of the class would create a risk of:

(A) Inconsistent or varying adjudications with respect to individual members of the class which would establish incompatible standards of conduct for the party opposing the class, or

(B) Adjudications with respect to individual members of the class which would as a practical matter be dispositive of the interests of the other members not parties to the adjudications or substantially impair or impede their ability to protect their interests; or

(2) The party opposing the class has acted or refused to act on grounds generally applicable to the class, thereby making appropriate final injunctive relief or corresponding declaratory relief with respect to the class as a whole; or

(3) The Court finds that the questions of law or fact common to the members of the class predominate over any questions affecting only individual members, and that a class action is superior to other available methods for the fair and efficient adjudication of the controversy. The matter pertinent to the findings include:

(A) The interest of members of the class in individually controlling the prosecution or defense of separate actions;

(B) The extent and nature of any litigation concerning the controversy already commenced by or against members of the class;

(C) The desirability or undesirability of concentrating the litigation of the claims in the particular forum;

(D) The difficulties likely to be encountered in the management of a class action.

(c) Determination by Order Whether Class Action to Be Maintained; Notice; Judgment; Actions Conducted Partially as Class Actions.

(1) As soon as practicable after the commencement of an action brought as a class action, the Court shall determine by order whether it is to be so maintained. An order under this paragraph may be conditional, and may be altered or amended before the decision on the merits.

(2) In any class action maintained under paragraph (b)(3), the Court shall direct to the members of the class the best notice practicable under the circumstances, including individual notice to all members who can be identified through reasonable effort. The notice shall advise each member that:

(A) The Court will exclude him from the class if he so requests by a specified date;

(B) The judgment, whether favorable or not, will include all members who do not request exclusion; and

(C) Any member who does not request exclusion may, if he desires, enter an appearance through his counsel.

(3) The judgment in an action maintained as a class action under paragraph (b)(1) or (b)(2), whether or not favorable to the class, shall include and describe those whom the Court finds to be members of the class. The judgment in an action maintained as a class action under paragraph (b)(3), whether or not favorable to the class, shall include and specify or describe those to whom the notice provided in paragraph (c)(2) was directed, and who have not requested exclusion, and whom the Court finds to be members of the class.

(4) When appropriate (A) an action may be brought or maintained as a class action with respect to particular issues, or (B) a class may be divided into subclasses and each subclass treated as a class, and the provisions of this rule shall then be construed and applied accordingly.

(d) Orders in Conduct of Actions. In the conduct of actions to which this rule applies, the Court may make appropriate orders: (1) Determining the course of proceedings or prescribing measures to prevent undue repetition or complication in the presentation of evidence or argument; (2) requiring, for the protection of the members of the class or otherwise for the fair conduct of the action, that notice be given in such manner as the Court directs to some or all of the members of any step in the action, or of the proposed extent of the judgment, or of the opportunity of members to signify whether they consider the representation fair and adequate, to intervene and present claims or defenses, or otherwise to come into the action; (3) imposing conditions on the representative parties or on

intervenors; (4) requiring that the pleadings be amended to eliminate therefrom allegations as to representation of absent persons, and that the action proceed accordingly; (5) dealing with similar procedural matters. The orders may be combined with an order under Rule 16, and may be altered or amended as may be desirable from time to time.

(e) Dismissal or Compromise. A class action shall not be dismissed or compromised without the approval of the Court, and notice by mail, publication or otherwise of the proposed dismissal or compromise shall be given to all members of the class in such manner as the Court directs; except that if the dismissa is to be without prejudice to the class or with prejudice to the plaintiff only, then such dismissal shall be ordered without notice thereof if there is a showing that no compensation in any form has passed directly or indirectly from any of the defendants to the plaintiff or plaintiff's attorney and that no promise to give any such compensation has been made.

APPENDIX H

Letter of Leslie Denend to Vitalink Stockholders, May 13, 1991, With Excerpts From Enclosures

May 13, 1991

TO THE STOCKHOLDERS OF VITALINK COMMUNICATIONS CORPORATION:

I am pleased to inform you that, effective as of May 6, 1991, Vitalink Communications Corporation ("Vitalink") entered into an Amended and Restated Agreement and Plan of Merger ("Agreement of Merger") providing for the acquisition of Vitalink by NSC Acquisition Corp. ("Purchaser"), a wholly-owned subsidiary of Network Systems Corporation ("NSC").

As required by the Agreement of Merger, Purchaser has commenced today a cash tender offer to purchase all outstanding shares of Vitalink Common Stock, including the associated Common Share Purchase Rights (the "Shares"), at a price of $10.50 per Share, net to the seller in cash, upon the terms and subject to the conditions set forth in an offer to purchase dated May 13, 1991 (the "Offer to Purchase") and related Letter of Transmittal (which together with the Offer to Purchase constitute the Offer). The Offer is currently scheduled to expire at 12:00 midnight, New York City time, on Monday, June 10, 1991.

Following the purchase of Shares under the Offer and satisfaction of certain other conditions, including such approval by Vitalink stockholders as may be required by law, Vitalink and Purchaser will merge (the "Merger") and each Share of Vitalink Common Stock not purchased in the Offer (other than Common Stock held by stockholders who have perfected any appraisal rights available under Delaware law) will be converted into the right to receive in cash $10.50 or such higher price per share of Common Stock as may have been paid in the Offer. Following con-

summation of the Merger, Vitalink Common Stock will no longer be publicly traded and will be owned by NSC.

The Offer is conditioned upon, among other things, there being validly tendered and not withdrawn before the expiration of the Offer a number of Shares which represents at least a majority of the total number of Shares outstanding at the time of purchase plus all Shares issued upon exercise of stock options which are exercisable on or before September 30, 1991.

The Board of Directors of Vitalink has unanimously approved each of the Offer and the Merger, has determined that the terms of each of the Offer and the Merger are fair to, and in the best interests of, the stockholders of Vitalink and recommends that Vitalink's stockholders accept the Offer and tender their Shares pursuant to the Offer.

In arriving at its recommendation, the Board of Directors has given careful consideration to a number of factors as described in the enclosed Schedule 14D-9 filed with the Securities and Exchange Commission, including the opinion of Kidder, Peabody & Co., Incorporated, Vitalink's financial advisor, that, as of the date of its opinion, the consideration to be received by the stockholders pursuant to the Agreement of Merger in the Offer and the Merger is fair to the stockholders from a financial point of view. The Schedule 14D-9 contains other important information relating to the Offer, and you are encouraged to read the Schedule 14D-9 carefully. Exhibits to the Schedule 14D-9 may be obtained from the Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549.

Accompanying this letter is the Offer to Purchase, together with related materials, including the Letter of Transmittal to be used for tendering your Shares. These documents set forth the terms and conditions of the Offer and provide instructions as to how to tender your Shares. We urge you to read the enclosed material carefully before

making your decision with respect to tendering your Shares in the Offer. If you have any questions or require assistance in tendering your Shares, you may contact Morrow & Co. Inc., the information Agent, at the telephone numbers and addresses listed in the Offer to Purchase.

On behalf of the Board of Directors and the management of Vitalink, we thank all of you for your support.

Sincerely,

/s/ Leslie G. Denend

LESLIE G. DENEND

Chairman of the Board of Directors, President and Chief Executive Officer

Excerpt from SEC Schedule 14D-9 Enclosed With Denend Letter of May 13, 1991

* * *

Litigation with Respect to the Offer.

Following the announcement of the execution of the Merger Agreement and the Offer on May 7, 1991, three putative class action suits, *John P. McCarthy Profit Sharing Plan v. Vitalink Communications Corporation et al.*, C.A. No. 12085, dated May 9, 1991, filed in the Court of Chancery of the State of Delaware, New Castle County, *Lara Ross Rubin v. Vitalink Communications Corporation et al.*, C.A. No. 12086, dated May 9, 1991, filed in the Court of Chancery of the State of Delaware, New Castle County, and *Chaille Steinberg et al. v. Vitalink Communications Corporation et al.*, C.A. No 12087, dated May 10, 1991, filed in the Court of Chancery of the State of Delaware, New Castle County, were filed by several alleged stockholders of the Company in the Court of Chancery of the State of Delaware, New Castle County (the "Delaware Litigation"). The Delaware Litigation names the Company, NSC and Leslie G. Denend as defendants.

In general, the Delaware Litigation alleges, among other things, that the consideration being offered for the Shares in the Offer is inadequate and that Mr. Denend and other members of the Company's management have breached their fiduciary duties by entering into a plan and scheme to sell the Company at an unfair price and perpetuate themselves in office and that NSC aided and abetted and induced such breaches of fiduciary duties. The Delaware Litigation further alleges that Mr. Denend and other members of the Company's management have breached their fiduciary duties by entering into the Stock Option Agreement and by not conducting an active auction of the Company.

The Delaware Litigation seeks, among other things, an injunction against the consummation of NSC's acquisition of the Shares and, in the event such acquisition is con-

summated, rescission of such acquisition. The Delaware Litigation also seeks an unspecified amount of compensatory damages, costs and attorneys' fees.

A putative class action suit, *Arnel Gonzalez v. Donald J. Herman et al.*, Case No. H 154853-0, dated May 8, 1991, filed in Superior Court for the State of California, County of Alameda, was filed by an alleged stockholder of the Company (the "California Litigation"). The California Litigation names the Company and certain of the Company's officers, directors and former directors as defendants.

The California Litigation alleges, among other state law claims, that certain of the defendants breached their fiduciary duties in connection with the Board's decision to enter into the Merger Agreement and, as a result of such conduct, the defendants were unjustly enriched at the expense of the Company's stockholders. The California Litigation seeks, among other things, injunctive relief, the appointment of a receiver to negotiate the sale of the Company and an unspecified amount of compensatory and punitive damages.

The Company and its counsel are reviewing the complaints described above. Copies of the complaints filed in the Delaware Litigation and the California Litigation are filed herewith as Exhibits 21 through 24 and are incorporated herein by reference.

* * *

Excerpt From "Offer To Purchase" Enclosed With Denend Letter of May 13, 1991

* * *

Litigation with Respect to the Offer. Following the announcement of the execution of the Merger Agreement and the Offer on May 7, 1991, three putative class action suits, *John P. McCarthy Profit Sharing Plan v. Vitalink Communications Corporation et al.*, C.A. No. 12085, dated May 9, 1991, filed in the Court of Chancery of the State of Delaware, New Castle County; *Lara Ross Rubin v. Vitalink Communications Corporation et al.*, C.A. No. 12086, dated May 9, 1991, filed in the Court of Chancery of the State of Delaware, New Castle County; and *Chaille Steinberg et al. v. Vitalink Communications Corporation et al.*, C.A. No. 12087, dated May 10, 1991, filed in the Court of Chancery of the State of Delaware, New Castle County, were filed by several alleged stockholders of the Company in the Court of Chancery of the State of Delaware, New Castle County (the "Delaware Litigation"). The Delaware Litigation names the Company, NSC and Leslie G. Denend as defendants.

In general, the Delaware Litigation alleges, among other things, that the consideration being offered for the Shares in the Offer is inadequate and that Mr. Denend and other members of the Company's management have breached their fiduciary duties by entering into a plan and scheme to sell the Company at an unfair price and perpetuate themselves in office and that NSC aided and abetted and induced such breaches of fiduciary duties. The Delaware Litigation further alleges that Mr. Denend and other members of the Company's management have breached their fiduciary duties by entering into the Stock Option Agreement and by not conducting an active auction of the Company.

The Delaware Litigation seeks, among other things, an injunction against the consummation of NSC's acquisition

of the Shares and, in the event such acquisition is consummated, rescission of such acquisition. The Delaware Litigation also seeks an unspecified amount of compensatory damages, costs and attorneys' fees.

Copies of the complaints described above are filed herewith as exhibits (g)(1), (g)(2) and (g)(3) and are incorporated herein by reference.

The Company has informed NSC that a putative class action suit, *Arnel Gonzales v. Donald J. Herman et al.*, Case No. H 154853-0, dated May 8, 1991, filed in Superior Court for the State of California, County of Alameda, was filed by an alleged stockholder of the Company (the "California Litigation"). The California Litigation names the Company and certain of the Company's officers, directors, former directors and consultants as defendants.

The California Litigation alleges, among other state law claims, that certain of the defendants breached their fiduciary duties in connection with the Board's decision to enter into the Merger Agreement and seeks both injunctive relief and unspecified damages. A copy of the complaint filed in the California Litigation is filed herewith as exhibit (g)(4) and is incorporated herein by reference.

* * *

APPENDIX I

Stipulation and Agreement of Compromise, Settlement, and Release

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

CONSOLIDATED
C.A. No. 12085

IN RE VITALINK COMMUNICATIONS CORPORATION SHAREHOLDERS LITIGATION

STIPULATION AND AGREEMENT OF COMPROMISE, SETTLEMENT AND RELEASE

The parties to the above-captioned action, as well as the parties to the California Actions (as defined below in paragraph 14) by and through their respective attorneys, propose the following Stipulation and Agreement of Compromise, Settlement and Release (the "Stipulation" or the "Settlement") for the Court's approval:

WHEREAS:

1. Defendant Vitalink Communications Corporation ("Vitalink") is a corporation organized and existing under the laws of the State of Delaware with its principal offices located at 6607 Kaiser Drive, Fremont, California. Vitalink designs, makes, markets and supports data communications products known as wide area bridges. Vitalink's stock trades over-the-counter on the National Association of Securities Dealers Automated Quotation System.

2. Defendant Network Systems Corporation ("NSC") is a corporation organized and existing under the laws of the

State of Delaware with offices in Minneapolis, Minnesota. It designs, manufactures, sells and services high performance data communications equipment used to connect a wide variety of mainframe computers, mini- computers and workstations.

3. NSC Acquisition Corp. is a wholly owned subsidiary of NSC.

4. In early 1990, Vitalink began to explore various strategic alternatives in reaction to increasingly competitive industry and market conditions. At that time NSC contacted Vitalink for the purpose of discussing a possible business relationship or combination of the two companies. In February 1990, Vitalink engaged Kidder, Peabody & Co. Incorporated ("Kidder, Peabody") to explore various financial and strategic alternatives on its behalf, including the possible sale of Vitalink. In April 1990, Vitalink instructed Kidder, Peabody to suspend its efforts related to Vitalink's strategic and financial alternatives, although discussions regarding potential transactions with NSC and other potential strategic partners continued.

5. In October 1990, Vitalink hired Leslie G. Denend as its President and Chief Executive Officer.

6. On December 10, 1990, NSC signed a Confidentiality Agreement obligating NSC to maintain the confidentiality of information received from Vitalink, thereby permitting a more detailed exchange of information between NSC and Vitalink. Representatives of the two companies met on December 10 and 11, 1990 to discuss potential synergies between the two companies and to further review the business and operations of Vitalink and NSC.

7. In January and early February 1991, NSC and Vitalink discussed the possibility of an original equipment manufacturing relationship between the two companies. In March 1991, the two companies determined that such a relationship was not the optimal way to capitalize upon

their strengths and that they should continue to explore a possible business combination. In February and March 1991, pursuant to the instructions of Vitalink's Board of Directors to consider other possible combinations, Denend and other representatives of Vitalink held discussions with two companies other than NSC. During these discussions, issues concerning the possible business combination of Vitalink with the other companies were considered. No firm proposal or expression of timely interest was received as a result of these discussions and, consequently, the discussions were terminated.

9. Vitalink began to confer again with Kidder, Peabody in March 1991 to discuss the strategic and financial alternatives available to Vitalink.

10. In March and April 1991, representatives of Vitalink and NSC held further discussions and meetings to exchange information and consider various structures and forms of consideration for a possible business combination. On April 18 and 19, 1991, representatives and advisors of NSC and Vitalink began extensive due diligence investigations.

11. On April 29, 1991, NSC proposed a transaction with Vitalink which would include a merger with NSC, pursuant to which Vitalink's stockholders would receive cash and NSC common stock equivalent to the trading price of Vitalink's stock. This offer was rejected by Vitalink's Board of Directors on April 30, 1991. On May 1, 1991, NSC increased its original offer to include a small premium, which offer was also rejected by Vitalink's Board of Directors.

12. Following further discussions between NSC and Vitalink, on May 1, 1991, NSC again increased its offer. The increased offer (the "Offer") included an acquisition by NSC Acquisition Corp. of all the outstanding shares of Vitalink pursuant to a cash tender offer at $10.50 per share, to be followed by a merger (the "Merger"), whereby

all remaining outstanding shares would be exchanged for the same cash consideration and NSC Acquisition Corp. would be merged into Vitalink. The terms of the Merger were set forth in an amended and restated merger agreement (the "Merger Agreement"). The Offer was subject to certain conditions, among them the condition that Vitalink grant NSC a common stock option for 19.9% of Vitalink's outstanding stock pursuant to a separate stock option agreement (the "Stock option Agreement"). The $10.50 per share Offer price represented a premium of approximately 23.5% over the closing price for Vitalink's common stock as of the last full trading day prior to the signing of the Merger Agreement.

13. On May 6, 1991, Vitalink's Board of Directors unanimously approved the Offer and the Merger, including the execution of the Merger Agreement and the Stock Option Agreement, determining that the terms of the Offer and the Merger were fair to, and in the best interests of, Vitalink's stockholders, and recommended that Vitalink's stockholders accept the Offer and approve and adopt the Merger Agreement.

14. On May 6, 1991, Vitalink and NSC announced that they had entered into the Merger Agreement. In response to the May 6, 1991 announcement, four separate lawsuits entitled *John P. McCarthy Profit Sharing Plan v. Vitalink Communications Corp., et al.*, Del. Ch., C.A. No. 12085 (May 9, 1991); *Rubin v. Vitalink Communications Corp., et al.*, Del. Ch., C.A. No. 12086 (May 10, 1991); *Steinberg v. Vitalink Communications Corp., et al.*, Del. Ch., C.A. No. 12087 (May 10, 1991); and *Arthur-Magna, Inc. v. Vitalink Communications Corp., et al.*, Del Ch., C.A. No. 12091 (May 13, 1991) (collectively, the "Delaware Actions") were filed in the Court of Chancery of the State of Delaware, in and for New Castle County (the "Court of Chancery"), challenging the proposed Merger on behalf of a putative class consisting of all Vitalink common stockholders (the "Class"). Three separate lawsuits entitled

Gonzales v. Vitalink Communications Corp., et al., C.A. No. 154853-0 (Alameda Super. Ct., May 8, 1991); *Clark v. Vitalink Communications Corp., et al.*, C.A. No. 154996-8 (Alameda Super. Ct., May 15, 1991; and *Shaine v. Vitalink Communications Corp. et al.*, C.A. No. 154995-9, dated May 15, 1991 (collectively, the "California Actions") were also filed in the Superior Court of the State of California for the County of Alameda, Southern Division, challenging the proposed Merger on behalf of the Class.

15. NSC Acquisition Corp. commenced the Offer to purchase for cash all outstanding shares of common stock of Vitalink at $10.50 net per share on May 13, 1991. The Offer was to expire at 12:00 midnight, EDT, on Monday, June 10, 1991. Vitalink filed a Schedule 14D-9 with the Securities and Exchange Commission on May 13, 1991.

16. Between May 13 and May 24, 1991, the parties engaged in extensive discovery in connection with a motion by the plaintiffs to enjoin preliminarily the consummation of the Offer. On May 28, 1991, in anticipation of this proposed Settlement, the plaintiffs withdrew their motion for a preliminary injunction then pending in the Court of Chancery.

17. On May 28, 1991, the Court consolidated the Delaware actions (the "Consolidated Action"). The Complaint in *John P. McCarthy Profit Sharing Plan v. Vitalink Communications Corp.*, Del. Ch., C.A. No. 10285, was designated as the complaint in the Consolidated Action.

18. The plaintiffs' counsel have conducted an investigation and evaluation of the facts and law relating to the matters set forth in the complaint in the Consolidated Action and the California Actions. This investigation has included the review of thousands of pages of documents, the depositions of two Vitalink representatives, including the Chairman of the Board and an outside director; a representative of Kidder, Peabody; the Chairman of the Board of NSC; and a representative of Salomon Brothers

Inc. ("Salomon"), NSC's investment banker. Having made such factual and legal investigation, the plaintiffs and their counsel have concluded that the terms of the Stipulation are fair, reasonable, adequate and in the best interests of the Class.

19. The plaintiffs and their counsel have agreed to the terms of the Settlement after considering: (i) the benefits that the plaintiffs and the other members of the Class will receive from the Settlement; (ii) the attendant risks of litigation; (iii) the probability of success on the merits of the allegations, including damages, contained in the Consolidated Action and the California Actions; (iv) the uncertainty relating to the proof of the allegations; (v) the desirability of permitting the Settlement to be consummated according to its terms; and (vi) their conclusion that the Settlement is in the best interests of all members of the Class and constitutes a fair, reasonable and adequate resolution of the litigation.

20. The defendants, and each of them, have at all times denied, and continue to deny, that they have committed, or have threatened to commit, any wrongful acts or violations of law of any nature whatsoever in connection with (i) any of the matters alleged, or which could have been alleged, in the Consolidated Action and the California Actions, (ii) any matter relating to NSC's acquisition of Vitalink or Vitalink stock, and (iii) any other aspect of Vitalink's business, operations or dealings with its stockholders. The defendants are entering into the Settlement because it will (i) halt the substantial expense, inconvenience and distraction of continued litigation of plaintiffs' claims, (ii) finally put to rest those claims, and (iii) dispel any uncertainty that may exist as a result of these litigations.

NOW, THEREFORE, IT IS STIPULATED AND AGREED, subject to the approval of the Court of Chancery, pursuant to Rule 23 of the Rules of the Court of Chancery, that

the Consolidated Action shall be dismissed on the merits with prejudice as to all the defendants and the Defendants' Affiliates (as defined below) and against the plaintiffs and all other members of the Class without costs, except as provided in the Stipulation. All claims, rights, causes of action, suits, matters and issues, known or unknown, that arise now or hereafter out of, or that relate to, or that are, were or could have been asserted in connection with, Vitalink's and NSC's employment agreements, change of control agreements, stock arrangements, and similar arrangements with Vitalink's employees, the Stock Option Agreement, NSC's proposals to acquire Vitalink stock (including, without limitation, the Offer, the Merger Agreement and the Merger), the disclosures made in the Schedule 14D-9, the Offer and the Merger, or any matters, transactions or occurrences referred to in the Complaint, or any other complaint in the Consolidated Action, or in any complaint in the California Actions, or any public statements, announcements or other activities relating to any of the foregoing, or the Settlement (except for an action to enforce compliance with the terms of the Settlement) (the "Settled Claims"), by any member of the Class or by Vitalink, either directly, individually, derivatively, representatively or in any other capacity against any of the defendants in the Consolidated Action, their respective present or former officers, directors, stockholders, agents, employees, attorneys, representatives, advisors, investment bankers (including, without limitation, Kidder, Peabody and Salomon and their officers, directors, agents and employees), commercial bankers, accountants, insurers, trustees, parents, affiliates, subsidiaries (direct and indirect, including, without limitation, NSC Acquisition Corp.), directors and officers of such parents, affiliates and subsidiaries, general and limited partners, heirs, executors, personal representatives, estates, administrators, successors and assigns (collectively, the "Defendants' Affiliates")

shall be compromised, settled, released and discharged subject to the following terms and conditions:

A. *The Offer.* The Offer, originally scheduled to expire on Monday, June 10, 1991 at 12:00 midnight, EDT, is extended ten days so that it shall not be scheduled to expire before Thursday, June 20, 1991 at 12:00 midnight, EDT.

B. *The Stock Option Agreement.* The Stock Option Agreement will be amended to (i) limit the Cancellation Amount (as defined in the Stock Option Agreement) payable to NSC to an amount not to exceed $2,771,311 (the number of Option shares multiplied by $1.00 per share) and (ii) provide that Vitalink will have the right to cancel the Option at any time after NSC has delivered to Vitalink an Exercise Notice (as defined in the Stock Option Agreement) provided the Option is then exercisable upon the payment to NSC of the Cancellation Amount. Such cancellation shall be in writing and Vitalink shall be obligated to pay NSC promptly (but, in any event, not more than ten business days) after giving NSC written notice of cancellation.

C. *The Merger Agreement.* Section 8.02(c) of the Merger Agreement will be amended to limit the reimbursement of NSC's fees and expenses by Vitalink to an amount not to exceed $1.75 million if NSC terminates the Merger Agreement pursuant to Section 8.01(b)(1).

D. *Notice of Settlement.* Notice of the extension of the Offer and amendments to the Merger Agreement and Stock Option Agreement shall be publicly announced as soon as practicable.

E. *Joint Application for Court Order.* As soon as practicable after the Stipulation has been executed, the parties hereto shall apply jointly to the Court of Chancery for an order with respect to notice, the Settlement hearing and Settlement administration (the "Order"):

(1) conditionally certifying the Class, solely for the purposes of the Settlement, pursuant to Court of Chancery Rules 23(a) and 23(b)(1) and/or (2), without the right of members of the Class to opt out, to include all record or beneficial holders of common stock of Vitalink, or their successors in interest, transferees and assigns, immediate and remote, who held shares at any time during the period from and including May 6, 1991 to and including the effective date of the Merger, excluding defendants, members of their immediate families, nominees and trusts and corporations controlled by them;

(2) providing that named plaintiffs in the Consolidated Action shall serve as the representative parties of the Class;

(3) directing that a hearing be held by the Court of Chancery (the "Settlement Hearing") to determine, among other things:

(a) whether the Court of Chancery should enter an order and final judgment in the Consolidated Action (the "Order and Final Judgment"), approving the Settlement pursuant to the Court of Chancery Rule 23(e) as fair, reasonable, adequate and in the best interests of the Class and Vitalink, and authorizing all acts necessary to consummate and effectuate the terms and conditions of this Stipulation;

(b) whether the Court of Chancery should enter the Order and Final Judgment, dismissing the Consolidated Action pursuant to Court of Chancery Rule 23(e) with prejudice and on the merits, each party to bear its own costs (except as expressly provided herein), and extinguishing and releasing any and all Settled Claims;

(c) whether, in the event that the Court of Chancery approves the Settlement, to pass upon any application by plaintiffs' counsel for an allowance for fees and reimbursement of expenses that they may make; and

(d) such other matters as the Court of Chancery may deem necessary and appropriate;

(4) providing that a copy of the Notice of Pendency of Class Action, Class Action Determination, Proposed Settlement of Class Action, Settlement Hearing and Right to Appear (the "Notice to the Class") be mailed by Vitalink via first-class mail within 14 days of the date of the Order, in the name of the Register in Chancery or by the direction of the Court of Chancery, to all Class members at their last known addresses appearing in the transfer journals of Vitalink (all costs associated with mailing the Notice to the Class shall be paid by Vitalink); and

(5) requesting all record holders in the Class who are not also the beneficial owners of the shares of Vitalink common stock held by them of record to forward the Notice to the Class to such beneficial owners of those shares. Additional copies of the Notice to the Class will be made to record holders for this purpose upon request directed to Vitalink, in care of:

Boris Feldman, Esquire
Wilson, Sonsini, Goodrich & Rosati
2 Palo Alto Square
Suite 900
Palo Alto, California 94306

F. *Order and Final Judgment of the Court.* Upon the determination of the Court of Chancery that the Settlement contained herein is fair, adequate, reasonable and in the best interests of the Class and Vitalink, the parties hereto jointly will move the Court of Chancery for entry of the Order and Final Judgment in the Consolidated Action. The Order and Final Judgment shall, among other things:

(1) approve the Settlement as fair, reasonable and adequate pursuant to Court of Chancery Rule 23(e);

(2) authorize and direct performance of the Settlement in accordance with its terms and conditions and reserve jurisdiction to supervise the consummation of the Settlement provided herein; and

(3) dismiss with prejudice the Consolidated Action and settle, discharge and release defendants, and each of them, and Defendants' Affiliates, from the Settled Claims.

G. *California Stipulation of Dismissal.* Within ten days of entry of the Order and Final Judgment, the parties to the California Actions shall jointly file a stipulation in the Superior Court of the State of California dismissing with prejudice the California Actions.

H. *Fee Application.* In connection with the presentation of the Settlement for approval by the Court, none of the defendants shall directly or indirectly oppose an application by the plaintiffs' counsel for an award of attorneys' fees not to exceed $275,000, and out-of-pocket expenses not to exceed $25,000, to be paid by Vitalink. The plaintiffs' counsel will not apply for an amount in excess of $275,000 for fees and $25,000 for expenses, and Vitalink shall pay to the plaintiffs' counsel such amount as may be awarded by the Court. The defendants reserve the right to oppose any other application made to the Court by any member of the Class or by any other person for an award of additional attorneys' fees and/or disbursements. The foregoing obligations of Vitalink shall be conditioned upon consummation of the Offer and approval of the Settlement by the Court in all respects, after any appeal from the Court's Order and Final Judgment shall have been finally decided, upholding in all respects the Court's approval of the Settlement, or after the time for the filing of any appeal shall have expired with no appeal having been commenced, and the dismissal with prejudice of the Consolidated Action and the California Actions. Payment shall be made to the plaintiffs' counsel by wire transfer within 5 business days of the time such conditions are met. If for

any reason payment is not made within five business days, interest shall be paid on the amount awarded by the Court at the prescribed legal statutory rate of interest until the fee is paid.

I. *Stipulation and Settlement Shall Not Constitute an Admission.* No provision contained in this Stipulation, nor any documents prepared or proceedings taken in connection with this Stipulation, shall be deemed an admission by any defendant as to any claim alleged or asserted or that could have been alleged or asserted in the Consolidated Action and the California Actions, and neither this Stipulation nor the negotiations or proceedings in connection with this Stipulation shall be offered or received in evidence at any action or proceeding of any nature or otherwise referred to or used in any manner in any court or other tribunal, except in an action or proceeding to enforce the terms or conditions of this Stipulation.

J. *Provisions if Settlement Not Approved by the Court of Chancery.* The Settlement is conditioned upon (a) final approval of the Settlement, including the certification of the Class, as provided for herein, pursuant to Court of Chancery Rules 23(a) and 23(b)(1) and/or (2), without the right of members of the Class to opt out, and (b) dismissal with prejudice of the Consolidated Action. In the event the Settlement proposed herein, including any amendment made in accordance with this Stipulation, is not approved by the Court, or the Court approves the Settlement but such approval is vacated on appeal and such order reversing or vacating the Settlement becomes final by lapse of time or because the order is no longer subject to any appeal or the Consolidated Action is not dismissed with prejudice, then the Settlement proposed herein shall be of no further force or effect, and the Settlement and any amendment thereof shall be null and void without prejudice to any party hereto, and each party shall be restored to his, her or its respective position as it existed prior to the execution of the Stipulation (except that all costs associ-

ated with mailing the Notice to the Class shall be paid by Vitalink).

K. *Amendment.* This Stipulation may not be amended, or any of its provisions waived, except by a writing executed by all of the parties hereto.

L. *Execution.* This Stipulation may be executed in one or more counterparts, all of which shall be considered one and the same agreement, and shall become effective when such counterparts have been signed by each of the parties and delivered to the other parties.

/s/ Joseph A. Rosenthal
Joseph A. Rosenthal
MORRIS, ROSENTHAL, MONHAIT & GROSS, P.A.
First Federal Plaza
P.O. Box 1070
Wilmington, Delaware 19899
(302) 656-4433
Delaware Plaintiffs' Liaison Counsel

/s/ Arthur N. Abbey
Arthur N. Abbey
ABBEY & ELLIS
212 E. 39th Street
New York, New York 10016
(212) 889-3700
Delaware Plaintiffs' Lead Counsel

/s/ Lester Levy
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845 Third Avenue
New York, New York 10022
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/s/ Randolph K. Herndon 6/13/91
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One Rodney Square
P.O. Box 636
Wilmington, Delaware 19899
(302) 651-3000
Attorneys for Defendant
Network Systems Corporation

DATED: June 10, 1991

APPENDIX J

Notice of Pendency of Class Action, Class Action Determination, Proposed Settlement, Settlement Hearing and Right To Appear

**IN THE COURT OF CHANCERY
OF THE STATE OF DELAWARE
IN AND FOR NEW CASTLE COUNTY**

**Consolidated
C.A. No. 12085**

IN RE VITALINK COMMUNICATIONS CORPORATION SHAREHOLDERS LITIGATION

NOTICE OF PENDENCY OF CLASS ACTION, CLASS ACTION DETERMINATION, PROPOSED SETTLEMENT, SETTLEMENT HEARING AND RIGHT TO APPEAR

TO: ALL HOLDERS OF COMMON STOCK OF VITALINK COMMUNICATIONS CORPORATION ("VITALINK" OR THE "COMPANY") AT ANY TIME DURING THE PERIOD FROM AND INCLUDING MAY 6, 1991 TO AND INCLUDING JULY 1, 1991, THE EFFECTIVE DATE OF THE MERGER (DEFINED BELOW), AND THEIR SUCCESSORS IN INTEREST, TRANSFEREES AND ASSIGNS, IMMEDIATE AND REMOTE.

THIS NOTICE IS TO INFORM YOU OF THE PROPOSED SETTLEMENT OF *IN RE VITALINK COMMUNICATIONS CORPORATION SHAREHOLDERS LITIGATION*, CONSOLIDATED C.A. NO. 12085 (THE "CONSOLIDATED ACTION"), AND THE HEARING TO BE HELD ON SEPTEMBER 16, 1991, AT 11:30 A.M., BEFORE THE HONORABLE WILLIAM B. CHANDLER, III, VICE CHANCELLOR OF THE COURT OF CHANCERY OF THE STATE OF DELAWARE (THE

"COURT OF CHANCERY") AT THE PUBLIC BUILDING, 11TH AND KING STREETS, WILMINGTON, DELAWARE, TO DETERMINE WHETHER THE STIPULATION AND AGREEMENT OF COMPROMISE, SETTLEMENT AND RELEASE ENTERED INTO BY THE PARTIES TO THE ABOVE CONSOLIDATED ACTION AND RELATED CALIFORNIA ACTIONS, DATED JUNE 10, 1991 (THE "SETTLEMENT" OR THE "STIPULATION"), IS FAIR, REASONABLE, ADEQUATE, IN THE BEST INTERESTS OF THE CLASS, AS DEFINED HEREIN, AND SHOULD BE APPROVED BY THE COURT; TO DETERMINE WHETHER JUDGMENT SHOULD BE ENTERED IN THE CONSOLIDATED ACTION PURSUANT TO THE SETTLEMENT, WHICH WILL, AMONG OTHER THINGS, DISMISS THE CONSOLIDATED ACTION WITH PREJUDICE; AND TO RULE ON SUCH OTHER MATTERS AS THE COURT MAY DEEM APPROPRIATE, INCLUDING ANY APPLICATION BY THE PLAINTIFFS' ATTORNEYS FOR FEES AND EXPENSES.

IF A PERSON OTHER THAN YOU WAS THE BENEFICIAL HOLDER OF SHARES OF VITALINK COMMON STOCK HELD BY YOU OF RECORD, YOU ARE REQUESTED TO FORWARD THIS NOTICE TO SUCH BENEFICIAL OWNER. ADDITIONAL COPIES OF THE NOTICE WILL BE MADE AVAILABLE TO YOU FOR THIS PURPOSE UPON REQUEST DIRECTED TO VITALINK COMMUNICATIONS CORPORATION, C/O:

RANDOLPH K. HERNDON, ESQUIRE
SKADDEN, ARPS, SLATE, MEAGHER & FLOM
ONE RODNEY SQUARE, P.O. BOX 636
WILMINGTON, DE 19899

PLEASE READ THIS NOTICE CAREFULLY. IF THE COURT APPROVES THE PROPOSED SETTLEMENT, YOU WILL BE FOREVER BARRED FROM CONTESTING THE FAIRNESS, REASONABLENESS OR ADEQUACY OF THE PROPOSED SETTLEMENT, OR FROM PURSUING THE SETTLED CLAIMS.

THE FOLLOWING RECITATION DOES NOT CONSTITUTE THE FINDINGS OF THE COURT OF CHANCERY. IT IS BASED ON REPRESENTATIONS MADE TO THE COURT OF CHANCERY BY COUNSEL FOR THE PARTIES.

BACKGROUND AND DESCRIPTION OF THE LITIGATION AND SETTLEMENT

1. Defendant Vitalink is a corporation organized and existing under the laws of the State of Delaware with its principal offices located at 6607 Kaiser Drive, Fremont, California. Vitalink designs, makes, markets and supports data communications products known as wide-area bridges. Before July 1, 1991, Vitalink's stock traded over-the-counter on the National Association of Securities Dealers Automated Quotation System.

2. Defendant Network Systems Corporation ("NSC" or "Network") is a corporation organized and existing under the laws of the State of Delaware with offices in Minneapolis, Minnesota. It designs, manufactures, sells and services high-performance data communications equipment used to connect a wide variety of mainframe computers, mini-computers and work stations.

3. NSC Acquisition Corp. is a wholly owned subsidiary of NSC.

4. In early 1990, Vitalink began to explore various strategic alternatives in reaction to increasingly competitive industry and market conditions. At that time NSC contacted Vitalink for the purpose of discussing a possible business relationship or combination of the two companies. In February 1990, Vitalink engaged Kidder, Peabody & Co. Incorporated ("Kidder, Peabody") to explore various financial and strategic alternatives on its behalf, including the possible sale of Vitalink. In April 1990, Vitalink instructed Kidder, Peabody to suspend its efforts related to Vitalink's strategic and financial alternatives, although dis-

cussions regarding potential transactions with NSC and other potential strategic partners continued.

5. In October 1990, Vitalink hired Leslie G. Denend as its President and Chief Executive Officer.

6. On December 10, 1990, NSC signed a Confidentiality Agreement obligating NSC to maintain the confidentiality of information received from Vitalink, thereby permitting a more detailed exchange of information between NSC and Vitalink. Representatives of the two companies met on December 10 and 11, 1990 to discuss potential synergies between the two companies and to further review the business and operations of Vitalink and NSC.

7. In January and early February 1991, NSC and Vitalink discussed the possibility of an original equipment manufacturing relationship between the two companies. In March 1991, the two companies determined that such a relationship was not the optimal way to capitalize upon their strengths and that they should continue to explore a possible business combination.

8. In February and March 1991, pursuant to the instructions of Vitalink's Board of Directors to consider other possible combinations, Denend and other representatives of Vitalink held discussions with two companies other than NSC. During these discussions, issues concerning the possible business combination of Vitalink with the other companies were considered. No firm proposal or expression of timely interest was received as a result of these discussions and, consequently, the discussions were terminated.

9. Vitalink began to confer again with Kidder, Peabody in March 1991 to discuss the strategic and financial alternatives available to Vitalink.

10. In early March 1991, Vitalink entered into change of control agreements with its seven executive officers and three key employees. The change of control agreements provided three types of benefits in connection with a

change of control of Vitalink. The three types of benefits triggered by a change of control were (a) enhanced severance benefits in connection with certain terminations of employment, (b) stock option acceleration and (c) payment of certain excise taxes.

11. In March and April 1991, representatives of Vitalink and NSC held further discussions and meetings to exchange information and consider various structures and forms of consideration for a possible business combination. On April 18 and 19, 1991, representatives and advisors of NSC and Vitalink began extensive due diligence investigations.

12. On April 29, 1991, NSC proposed a transaction with Vitalink that would have included a merger with NSC, pursuant to which Vitalink's stockholders would receive cash and NSC common stock equivalent to the trading price of Vitalink's stock. This offer was rejected by Vitalink's Board of Directors on April 30, 1991. On May 1, 1991, NSC increased its original offer to include a small premium to the trading price of Vitalink stock, which offer was also rejected by Vitalink's Board of Directors.

13. Following further discussions between NSC and Vitalink, on May 1, 1991, NSC again increased its offer. The increased offer (the "Offer") included an acquisition by NSC Acquisition Corp. of all the outstanding shares of Vitalink pursuant to a cash tender offer at $10.50 per share, to be followed by a merger (the "Merger"), whereby all remaining outstanding shares would be exchanged for the same cash consideration, and NSC Acquisition Corp. would be merged into Vitalink. The terms of the Merger were set forth in an amended and restated merger agreement (the "Merger Agreement"). The Offer was subject to certain conditions, among them the condition that Vitalink grant NSC a common stock option to purchase for $10.50 per share stock representing approximately 19.9% of Vitalink's outstanding stock pursuant to a separate stock

option agreement (the "Stock Option Agreement"). The $10.50 per share Offer price represented a premium of approximately 23.5% over the closing price for Vitalink's common stock as of the last full trading day prior to the signing of the Merger Agreement.

14. On May 6, 1991, Vitalink's Board of Directors unanimously approved the Offer and the Merger, including the execution of the Merger Agreement and the Stock Option Agreement, determining that the terms of the Offer and the Merger were fair to, and in the best interests of, Vitalink's stockholders, and recommended that Vitalink's stockholders accept the Offer and approve and adopt the Merger Agreement.

15. On May 6, 1991, Vitalink and NSC announced that they had entered into the Merger Agreement. In response to the May 6, 1991 announcement, four separate lawsuits, entitled *John P. McCarthy Profit Sharing Plan v. Vitalink Communications Corp., et al.*, Del. Ch., C.A. No. 12085 (May 9, 1991); *Rubin v. Vitalink Communications Corp., et al.*, Del. Ch., C.A. No. 12086 (May 10, 1991); *Steinberg v. Vitalink Communications Corp., et al.*, Del Ch. C.A. No. 12087 (May 10, 1991); and *Arthur-Magna, Inc. v. Vitalink Communications Corp., et al.*, Del Ch., C.A. No. 12091 (May 13, 1991) (collectively, the "Delaware Actions"), were filed in the Court of Chancery, challenging the proposed Merger on behalf of a putative class consisting of all Vitalink common stockholders (the "Class"). Three separate lawsuits entitled *Gonzales v. Vitalink Communications Corp., et al.*, C.A. No. 154853-0 (Alameda Super. Ct. May 8, 1991); *Clark v. Vitalink Communications Corp., et al.*, C.A. No. 154996-8 (Alameda Super. Ct. May 15, 1991); and *Shaine v. Vitalink Communications Corp., et al.*, C.A. No. 154995-9 (Alameda Super. Ct. May 15, 1991) (collectively, the "California Actions"), were also filed in the Superior Court of the State of California for the County of Alameda, Southern Division, challenging the proposed Merger on behalf of the Class.

16. In general, the Delaware Actions alleged, among other things, that the consideration being offered for the Vitalink shares in the Offer was inadequate and that members of Vitalink's management had breached their fiduciary duties by entering into a plan and scheme to sell Vitalink at an unfair price and perpetuate themselves in office, and that NSC aided and abetted and induced such breaches of fiduciary duties. The Delaware Actions further alleged that members of Vitalink management had breached their fiduciary duties by entering into a stock option agreement with NSC and by not conducting an active auction of the Company.

17. The California Actions generally alleged that the officers and directors of Vitalink were engaged in a wrongful course of conduct, were attempting to entrench and/or enrich themselves in "their lucrative positions of power, prestige and profit" with Vitalink, and were "refusing to offer in good faith a sale of the Company at a premium price through competitive bidding by any person." In addition, the California plaintiffs alleged that the defendants' wrongful acts were forcing the Class members to consider "only the Network tender offer at $10.50 per share, a price below the fair value" of Vitalink stock, and thus defendants' wrongful acts were "wrongfully tortiously interfering with the potential advantageous sale" of Vitalink stock through "competitive bidding at a premium price." The California Actions also alleged that the defendants had "wrongfully misappropriated corporate information to their own profit and benefit, and had failed to make full disclosure to shareholders of all material facts regarding the acquisition by Network and to disclose such information to other potential bidders." The complaints also challenged a "20% stock option granted to Network" claiming that it "all but guaranteed the success of Network's tender offer to acquire at least a majority" of Vitalink's outstanding stock.

18. NSC Acquisition Corp. commenced the offer to purchase for cash all outstanding shares of common stock of Vitalink at $10.50 net per share on May 13, 1991. The Offer was originally scheduled to expire at 12:00 midnight, Eastern Daylight Savings Time ("EDT"), on Monday, June 10, 1991. Vitalink filed a Schedule 14D-9 with the Securities and Exchange Commission on May 13, 1991.

19. Between May 13 and May 24, 1991 the parties in the Delaware Actions engaged in discovery in connection with a motion by the Delaware plaintiffs to enjoin preliminarily the consummation of the Offer. On May 28, 1991, in anticipation of this proposed Settlement, the Delaware plaintiffs withdrew their motion for a preliminary injunction.

20. On May 28, 1991, the court consolidated the Delaware Actions (the "Consolidated Action"). The complaint in *John P. McCarthy Profit Sharing Plan v. Vitalink Communications Corp.*, Del. Ch., C.A. No. 10285, was designated as the complaint in the Consolidated Action.

21. On Thursday and Friday, May 29 and 30, the parties in the Consolidated Actions executed a Stipulation and Agreement of Compromise, Settlement and Release ("Stipulation I"). Vitalink and NSC announced the terms of the proposed settlement on Monday, June 3, 1991. Later, during the week of June 10, 1991, the plaintiffs in the California Actions, along with the parties to the Consolidated Action, executed the Stipulation. The Stipulation generally provides for the same terms of settlement as was provided in Stipulation I, except that the Stipulation provides for an express release of the California Actions. The Stipulation was fully executed June 13, 1991, and its terms were publicly announced on Friday, June 14, 1991.

22. After the Offer expired on June 20, 1991 and the shares were purchased pursuant to the terms of the Offer, NSC and NSC Acquisition Corporation collectively owned approximately 90.7% of the outstanding shares of Vita-

link's common stock. On July 11, 1991, NSC mailed a Notice of Merger to the former stockholders of Vitalink who did not tender their shares in the Offer, that pursuant to Sections 253(d) and 262(d) of the General Corporation Law of the State of Delaware ("Delaware Corporation Law") the Merger became effective on July 1, 1991. Under applicable Delaware Corporation Law, no action was required by Vitalink stockholders (other than by NSC and NSC Acquisition Corporation) for the Merger to become effective.

23. The plaintiffs' counsel have conducted a thorough investigation and evaluation of the facts and law relating to the matters set forth in the complaint in the Consolidated Action and the California Actions. This investigation has included the review of thousands of pages of documents; the depositions of two Vitalink representatives, including the Chairman of the Board and an outside director; and the depositions of a representative of Kidder, Peabody, the Chairman of the Board of NSC and a representative of Salomon Brothers Inc ("Salomon"), NSC's investment banker. Having made such factual and legal investigation, the plaintiffs and their counsel have concluded that the terms of the Stipulation are fair, reasonable, adequate and in the best interests of the Class.

24. The plaintiffs and their counsel have agreed to the terms of the Settlement after considering: (i) the benefits that the plaintiffs and the other members of the Class will receive from the Settlement, (ii) the attendant risks of litigation; (iii) the probability of success on the merits of the allegations, including damages, contained in the Consolidated Action and California Actions; (iv) the uncertainty relating to the proof of the allegations contained in the Consolidated Action and California Actions; (v) the desirability of permitting the Settlement to be consummated according to its terms; and (vi) their conclusion that the Settlement is in the best interests of all members of

the Class and constitutes a fair, reasonable and adequate resolution of the litigations.

25. The defendants, and each of them, have at all times denied, and continue to deny, that they have committed, or have threatened to commit, any wrongful acts or violations of law of any nature whatsoever in connection with (i) any of the matters alleged, or which could have been alleged, in the Consolidated Action and California Actions, (ii) any matter relating to NSC's acquisition of Vitalink or Vitalink stock, and (iii) any other aspect of Vitalink's business, operations or dealings with its stockholders. The defendants are entering into the Settlement because it will (i) halt the substantial expense, inconvenience and distraction of continued litigation of plaintiffs' claims, (ii) finally put to rest those claims, and (iii) dispel any uncertainty that may exist as a result of these litigations.

26. The proposed Settlement is now pending before The Honorable William B. Chandler, III, Vice Chancellor of the Court of Chancery. If approved by the Court of Chancery, the Settlement would be binding on the Class, which has been certified by the Court of Chancery for purposes of settlement only, consisting of all record or beneficial holders of common stock of Vitalink, and their successors in interest or transferees and assigns, immediate and remote, who held shares at any time during the period from and including May 6, 1991 to and including July 1, 1991, the effective date of the Merger, excluding defendants, members of their immediate families, nominees and trusts and corporations controlled by them.

27. The Settlement is in consideration of the following benefits conferred upon the Class:

A. *The Offer*. The Offer, originally scheduled to expire on Monday, June 10, 1991, at 12:00 midnight, EDT, was extended ten days so that it would not be scheduled to expire before Thursday, June 20, 1991, at 12:00 midnight, EDT.

B. *The Stock Option Agreement.* The Stock Option Agreement was amended to (i) limit the Cancellation Amount (as defined in the Stock Option Agreement) payable to NSC to an amount not to exceed $2,771,331 (the number of Option shares multiplied by $1.00 per share) and (ii) provide that Vitalink would have the right to cancel the Option at any time after NSC had delivered to Vitalink an Exercise Notice (as defined in the Stock Option Agreement) and that the Option would be then cancelled upon the payment to NSC of the Cancellation Amount. Such cancellation would have been required to be in writing and Vitalink would have been obligated to pay NSC promptly (but, in any event, not more than ten business days) after giving NSC written notice of cancellation.

C. *The Merger Agreement.* Section 8.02(c) of the Merger Agreement was amended to limit the reimbursement of NSC's fees and expenses by Vitalink to an amount not to exceed $1.75 million if NSC terminated the Merger Agreement pursuant to Section 8.01(b)(1).

D. *Notice of Settlement.* Notice of the extension of the Offer and amendments to the Merger Agreement and Stock Option Agreement were required to be publicly announced as soon as it was practicable (such announcements were made on June 3, 1991 and June 14, 1991).

DISMISSAL OF THE CONSOLIDATED ACTION AND RELEASE OF CLAIMS

28. The Stipulation provides that if the Settlement is approved by the Court of Chancery, the Consolidated Action shall be dismissed on the merits with prejudice as to all the defendants and the Defendants' Affiliates (as defined below) and against the plaintiffs and all other members of the Class without costs, except as provided in the Stipulation. All claims, rights, causes of action, suits, matters and issues, known or unknown, that arise now or

hereafter out of, or that relate to, or that are, were or could have been asserted in connection with, Vitalink's and NSC's employment agreements, change of control agreements, stock arrangements and similar arrangements with Vitalink's employees, the Stock Option Agreement, NSC's proposals to acquire Vitalink stock (including, without limitation, the Offer, the Merger Agreement and the Merger), the disclosures made in the Schedule 14D-9, the Offer and the Merger, or any matters, transactions or occurrences referred to in the complaints, or any other complaint in the Consolidated Action, or in any complaint in the California Actions, or any public statements, announcements or other activities relating to any of the foregoing, or the Settlement (except for an action to enforce compliance with the terms of the Settlement or an action for appraisal rights under Sections 253(d) and 262 of the Delaware General Corporation Law) (the "Settled Claims"), by any member of the Class or by Vitalink, either directly, individually, derivatively, representatively or in any other capacity against any of the defendants in the Consolidated Action, their respective present or former officers, directors, stockholders, agents, employees, attorneys, representatives, advisors, investment bankers, (including, without limitation, Kidder, Peabody and Salomon and their officers, directors, agents and employees), commercial bankers, accountants, insurers, trustees, parents, affiliates, subsidiaries (direct and indirect, including, without limitation, NSC Acquisition Corp.), directors and officers of such parents, affiliates and subsidiaries, general and limited partners, heirs, executors, personal representatives, estates, administrators, successors and assigns (collectively, the "Defendants' Affiliates"), shall be compromised, settled, released and discharged.

THE SETTLEMENT HEARING

29. All members of the Class have an interest in the Consolidated Action and California Actions and are hereby

notified that a hearing will be held before the Court of Chancery at the Public Building, 11th and King Streets, Wilmington, Delaware, on September 16, 1991, at 11:30 a.m. (the "Settlement Hearing"), to determine whether: (i) the Stipulation is fair, reasonable, adequate and in the best interests of the Class, and should be approved by the Court of Chancery; (ii) an Order and Final Judgement, as contemplated by the Settlement, should be entered dismissing the Consolidated Action as to all defendants and with prejudice as against the named plaintiffs and all members of the Class, and (iii) if the Court of Chancery approves the Settlement, and enters the Order and Final Judgment, the Court of Chancery should grant the application of the plaintiffs' attorneys for attorneys' fees and expenses.

30. The Court of Chancery has reserved the right to adjourn the Settlement Hearing from time to time by oral announcement at such hearing or during any adjournment thereof, without further notice of any kind. The Court of Chancery also has reserved the right to approve the Settlement with or without modification, to enter an Order and Final Judgment dismissing the Consolidated Action on the merits and with prejudice, and to order the payment of attorneys' fees and disbursements without further notice of any kind.

THE CALIFORNIA STIPULATION OF DISMISSAL

31. The Stipulation also provides that if the Settlement is approved by the Court of Chancery, within ten days of entry of the Order and Final Judgment, the parties to the California Actions shall jointly file a stipulation in the Superior Court of the State of California dismissing with prejudice the California Actions.

APPLICATION FOR ATTORNEYS' FEES AND EXPENSES

32. If the Settlement is approved by the Court of Chancery in all respects, the plaintiffs' attorneys will apply to

the Court of Chancery for an award of attorneys' fees not to exceed $275,000 and out-of-pocket expenses not to exceed $25,000. As provided in the Stipulation, the defendants have agreed not to oppose an application for fees and expenses for such amounts. (Stipulation I provided that the defendants would not oppose an application for an award of attorneys' fees so long as the application did not seek fees in an amount in excess of $200,000.) Subject to the conditions set forth in the Stipulation, including approval of the Settlement by the Court of Chancery in all respects and the dismissal with prejudice of the Consolidated Action and California Actions, Vitalink will pay the plaintiffs' counsel such fees and expenses as may be awarded by the Court of Chancery. The defendants reserve the right to oppose any other application made to the Court of Chancery by any member of the Class or by any other person for an award of additional attorneys' fees and/or disbursements.

RIGHT TO APPEAR

33. At the Settlement Hearing, any person who objects to the Settlement, the judgment to be entered in the Consolidated Action, or the award of attorney's fees and expenses, may appear in person or by his attorney at the hearing and present any evidence or arguments that may be proper and relevant; provided, however, that no person other than the named plaintiffs and the defendants in the Consolidated Action and California Actions shall be heard and no papers, briefs, pleadings or other documents submitted by any such person shall be received and considered by the Court of Chancery (unless the Court of Chancery in its discretion shall thereafter otherwise direct, upon application of such person and for good cause shown), unless no later than ten (10) days prior to the Settlement Hearing such person files with the Court and serves upon counsel listed below: (a) a written notice of intention to appear, (b) a statement of such person's objections to any

matters before the Court of Chancery, and (c) the grounds therefor or the reasons that such person desires to appear and to be heard, and all documents or writings that such person desires the Court of Chancery to consider:

Joseph A. Rosenthal, Esquire
Morris, Rosenthal, Monhait & Gross, P.A.
First Federal Plaza
P.O. Box 1070
Wilmington, Delaware 19899

Arthur N. Abbey, Esquire
Abbey & Ellis
212 E. 39th Street
New York, New York 10016

Lester Levy, Esquire
Wolf, Popper, Ross, Wolf & Jones
845 Third Avenue
New York, New York 10022

Randolph K. Herndon, Esquire
Skadden, Arps, Slate, Meagher & Flom
One Rodney Square
P.O. Box 636
Wilmington, Delaware 19899

Bruce M. Stargatt, Esquire
Young, Conaway, Stargatt & Taylor
11th Floor, Rodney Square North
P.O. Box 551
Wilmington, Delaware 19899

34. Unless the Court of Chancery otherwise directs, no person will be entitled to object to the approval of the Settlement, the judgment to be entered in the Consolidated Action and California Actions, or the award of attorneys' fees and expenses to plaintiffs' counsel, or otherwise to be heard, except by serving and filing written objections as described above. Any person who fails to object in the

manner prescribed above will be deemed to have waived such objection and will be forever barred from raising such objection in this action. Pending final determination of whether the Settlement should be approved, the Court of Chancery has ordered that the plaintiffs, all members of the Class, or any of them, either directly, representatively or in any capacity, upon the receipt of this Notice, may not commence or prosecute any action asserting claims that are or relate to the Settled Claims.

SCOPE OF THIS NOTICE

35. The foregoing description of the transaction at issue, the litigations, the Settlement Hearing, the Consolidated Action, the California Actions, the Class determination, the terms of the proposed Settlement and other matters described herein, does not purport to be comprehensive. Members of the Class are referred to the Stipulation and documents filed with the Court of Chancery in the Consolidated Action, and documents filed in the Superior Court of the State of California for the County of Alameda, including the pleadings and other papers, which you or your attorney may examine during regular business hours of each business day at the offices of the Register in Chancery, Public Building, 11th and King Streets, Wilmington, Delaware 19801, and the Alameda County Superior Court, Southern Division, 24405 Amador Street, Room 108, Hayward, California 94544.

DATED: Wilmington, Delaware
July 18, 1991

/s/ John D. Kelly, III
John D. Kelly, III
Register in Chancery

APPENDIX K

Excerpt From "Plaintiffs' Memorandum of Law in Support of Proposed Settlement and in Support of Application for Attorneys' Fees and Expenses and in Opposition to Objection" Before the Delaware Court of Chancery

* * *

Plaintiffs' counsel expended over 500 hours in litigation, negotiation, and settlement of this case, and through the present have incurred expenses of over $20,000. In working on the case, plaintiffs' counsel were mindful to avoid duplication of effort or any unnecessary work.

* * *

APPENDIX L

Excerpts From "Memorandum of Objectors in Opposition to Proposed Settlement" Before the Delaware Court of Chancery

* * *

Finally, in numerous crucial respects the record presented to the Court by the parties is far too undeveloped to justify approval of the proposed settlement.

This settlement is not fair to the class. This Court should decline any invitation to approve the defendants' efforts to be rid of this litigation by paying off the plaintiffs' attorneys, providing sham benefits to the class and cutting off forever the ability of the absent members of the class to pursue their rights.

* * *

[15] Objectors requested that class counsel respond to certain specific questions regarding the proposed settlement, including the alleged benefits conferred upon the class. *See* letter from Gregory P. Williams, Esquire to Lee Squitieri, Esquire dated August 27, 1991 (attached as Exhibit E hereto [see p. 94a *infra*]). Counsel has not responded to those questions.

* * *

With respect to certain of the areas covered in the stipulation, there was little or no discovery. For example, as discussed above, plaintiffs did not even assert disclosure claims and took no discovery in aid thereof. As to those areas where there was discovery, as pointed out herein, that discovery was in large part ineffective. In any event, in light of the non-existent benefits being offered to the members of the class, this Court should not deprive the class members of their rights to protect their interests in an effective and determined manner.

* * *

The record in the present case is sparse, to say the least. Five depositions were taken—two of them were less than 100 pages in length and one was less than 50. Objectors recognize that the volume of discovery is not necessarily indicative of the substance—but here the substance also is lacking. Objectors will not burden the Court with the literally hundreds of material questions which went unasked in the depositions. Instead, objectors list below a sampling of areas as to which little or no discovery occurred:

- No discovery occurred as to why there was no disclosure of the fact that Kidder had not solicited bids from third parties. No discovery occurred as to why the Kidder opinion disseminated to the Vitalink stockholders did not contain the statement contained in the draft of the opinion that Kidder had not been requested to solicit third parties;
- No discovery occurred as to the discrepancies discussed above in the Kidder discounted cash flow valuation;
- The deposition of Valdez of Kidder does not contain an explanation of the rationale for Kidder's March 15 recommendation that a confidential auction was in the best interests of the Company or the rationale for Kidder's contrary recommendation on April 9. Denend, to whom both those presentations were made, was asked about neither the March 15 recommendation nor the April 9 recommendation;
- While the minutes of the April 9 meeting of the board of directors state that the board discussed potential strategic partners for Vitalink including "[A,B] and others," sparse discovery occurred as to the substance of the board's dis-

cussions as to [A] and the "others." Denend, chairman of the board, was asked no questions regarding those discussions.

- Very little discovery occurred as to the discussions between NSC and Vitalink regarding the Stock Option Agreement, with no discovery having been taken of NSC as to the manner in which NSC had arrived at the various terms of the option in formulating its proposal. Indeed, plaintiff's counsel failed to ask Lyle Altman, chairman of NSC, a single question regarding the Stock Option Agreement;

- Very little discovery occurred as to the discussions between the parties regarding the "no-shop" clause and no questions were posed to either Altman or McNamara of Salomon (the only two representatives of NSC plaintiffs deposed) regarding the "no-shop" clause. Thus, neither Altman nor McNamara were asked whether NSC would have withdrawn its offer had Vitalink insisted on conducting a confidential auction;

- The record contains no evidence as to why the tender offer and 14D-9 contained no discussion of the various valuation methodologies employed by Kidder, the results derived by Kidder or the limitations in those valuation methodologies.

- No questions were asked of McNamara of Salomon as to why Salomon did not employ the comparable company analysis relied upon so heavily by Kidder and the Vitalink board;

- Chairman Denend was asked no questions regarding the discussions which purportedly occurred at the May 5 and May 6 meetings of

the board of directors regarding the advisability of attempting to solicit third-party bids.

The depositions in this action all occurred in a three-day period. At the time, such expedition was warranted. There is no reason now, however, for this Court to approve a settlement where questions highly important to the claims purportedly asserted on behalf of the Class remain unanswered.

* * *

Exhibit E (Letterhead omitted)

August 27, 1991

VIA TELECOPY

Lee Squitieri, Esquire
Abbey & Ellis
212 East 39th Street
New York, New York 10016

Re: In re Vitalink Communications Corporation Shareholders Litigation

Dear Lee:

This letter is to follow up on our telephone conversation last Friday where we discussed the proposed settlement of the litigation captioned *In re Vitalink Communications Corporation Shareholders Litigation*, Cons. C.A. No. 12085. In that conversation, you stated, among other things, that you would not respond to certain of my questions until my client had agreed to adhere to the confidentiality stipulation entered in the case. I attach hereto Mr. Grimes' signed statement that he will do so.

To provide us additional information to consider in determining whether to object to the proposed settlement,

I would request that you, on behalf of plaintiffs, respond in writing to the following items:

1. Please state the date settlement was first discussed between any of the plaintiffs, on the one hand, and any of defendants, on the other, or their respective representatives.

2. Please state the date any agreement in principle or similar understanding was reached between any of the plaintiffs, on the one hand, and any of the defendants, on the other, or their respective representatives.

3. Please state the date that the possibility of the payment of plaintiffs' attorneys' fees was first discussed between any of the plaintiffs, on the one hand, and any of the defendants, on the other, or their respective representatives.

4. Please state the manner in which the following aspects of the proposed settlement agreement conferred benefits upon the class:

   (a) extension of the Offer for ten days so that it would not be scheduled to expire before Thursday, June 20, 1991, at 12:00 midnight;

   (b) amendment of the Stock Option Agreement to limit the Cancellation Amount payable to NSC to an amount not to exceed $2,771,311.00;

   (c) amendment of the Stock Option Agreement to provide that Vitalink would have the right to cancel the Option at any time after NSC had delivered to Vitalink an Exercise Notice and that the Option would be then cancelled upon the payment to NSC of the Cancellation Amount;

   (d) amendment of the Merger Agreement to limit the reimbursement of NSC's fees and expenses

by Vitalink to an amount not to exceed $1.75 million if NSC terminated the Merger Agreement pursuant to Section 8.01(b)(1);

(e) the requirement that notice of the extension of the Offer and amendments to the Merger Agreement and Stock Option Agreement be publicly announced as soon as it was practicable.

5. Please state whether plaintiffs or their counsel had knowledge at the time the settlement agreement was entered into of any entity, other than NSC, then considering purchasing Vitalink. If so, please identify such entity or entities and state whether plaintiffs or their counsel had knowledge as to whether each such entity had expressed any concern regarding the Stock Option Agreement.

6. Please state plaintiffs or their counsels' beliefs as to the strengths and weaknesses of plaintiffs' claim that the $10.50 price of the Offer and Merger was inadequate and that members of Vitalink's management had breached their fiduciary duties by agreeing to sell Vitalink at such price.

7. Please identify any of plaintiffs' individually numbered requests for production of documents as to which defendants did not produce all responsive documents.

8. Please describe any documents identified by defendants to plaintiffs as having been withheld from production pursuant to a claim of privilege.

Capitalized terms above are used in accordance with the definitions of those terms set forth in the Notice of Proposed Settlement. I would also request that you send to me a copy of any memorandum of understanding entered into between the parties prior to the settlement agreement submitted to the Court for approval, as well as the doc-

ument referred to in the notice as "Stipulation I." In addition, please send to me copies of the California complaints.

I would appreciate your response by the close of business on Friday, August 30, 1991.

Very truly yours,

/s/ Gregory P. Williams
Gregory P. Williams

GPW/kdm

cc: Steven J. Rothschild, Esquire
Mr. Charles L. Grimes

APPENDIX M

Excerpts From Transcript of Settlement Hearing and Request for Attorneys' Fees Before the Delaware Court of Chancery

[Tr. 4] THE COURT: . . . I need [Tr. 5] some but not all of the submissions of those who are proposing the settlement. I have not yet had a chance to read the papers in opposition to the settlement, mainly because there was a problem with getting those transmitted down to Georgetown for me to review. But I have had a chance to review most of the things. I am familiar with the basics of the transaction and the settlement.

* * *

[Tr. 49] MR. WILLIAMS: . . . Nobody knows what the other side of the story is. Where is the plaintiffs' banker? Did they have a banker? Did they have somebody to evaluate the banker's work, the opposing banker's work, to say how strong their claims were, somebody telling them, "Hey, you can tear that guy apart"? I don't think they did. Maybe they did and haven't bothered to put in the [Tr. 50] evidence. I don't think that's the case.

* * *

[Tr. 51] The other thing, Your Honor, where in the record is the response of management to these projections? Where is the chief financial officer? He was mentioned in the deposition, Wes Saia. He presumably was instrumental in preparing these projections. If I'm the plaintiff and I've somebody telling me this range is high because these projections are unrealistic, I want to talk to the guy that prepared them. That's not in the record, Your Honor.

* * *

[Tr. 64] Your Honor, I submit that the defendants knew at least that there wasn't going to be anybody coming forward under this circumstance, so this change to the stock option agreement, it was meaningless. You know [Tr.

65] what it does? It enables us to play the game that people have criticized Delaware and its courts for. That is, "We'll pay off these guys, pay off the attorneys. We do something that is meaningless, that doesn't cost us a penny, and we know it's not going to affect us, and we are rid of this litigation and we forever bar the class members from suing us, and we get the release as wide as we can." That's what they did.

* * *

[Tr. 66] Then I asked other sort of, I thought, innocuous questions, like, "When did you agree to a settlement? You represent my clients. When was there a deal? Was there a memorandum of understanding?" He said there was. Sent him the letter. I asked for the memorandum of understanding. You will see the letter. I think there is—if I was class counsel, I would want to answer these questions. I never got an answer back. Then I wrote—I called him that following week.

I don't like to do this, Your Honor, because it's sort of like kissing and telling, but it's a very material transaction to my clients here. I do this advisedly and reluctantly, but I then wrote to Mr. Squitieri. I asked him: "You haven't responded to my [Tr. 67] calls now twice. Please answer my letter and please respond to my calls." I never heard from him. I don't understand that, both as a member of the Bar and somebody—his firm practices before this Court frequently. Much of this information—

I then thought they are not going to tell me, but this is all going to be put forward in the paper. Maybe there is a timing advantage. They will inform the Court when all this happened. They didn't. My questions went to, really, "What is in this settlement for my clients," as well as, "What kind of settlement was it? When did you do it? How real was this discovery?" I got no response. I didn't even get what I considered basic professional courtesy.

* * *

[Tr. 68] There were five depositions. They happened real quickly. They happened in three days. I understand that expedition was necessary and warranted, and nobody's perfect, but the expedition passed. There was a chance to find out. That's the way it often happens when there is an agreement in principle. Then you do confirmatory discovery, and sometimes that confirmatory discovery is real. You are looking to see, "Do you have a claim?" That didn't happen here.

They were content with their five depositions. If you read these depositions—I couldn't ever prove it, but for example, you read the [Tr. 69] last two depositions, critical depositions, Mr. Denend and Mr. Altman. They happened on Friday, the same day. Mr. Altman's, I think, started at around 7:50 in the morning. It's over at 9:10. It's a 44-page deposition. This is the chairman, the negotiator for the acquiror. How in the world could you take his deposition in 44 pages? Maybe those 44 pages were brilliant and you cut to the quick on everything, but if you read that deposition, you will see that is not a fully-developed deposition.

Mr. Rothschild, to his credit, asked a question at the end, because, again, amazingly to me, the plaintiffs didn't ask the chairman of NSC any questions about the stock option agreement. This is the big, you know, "They forced this on us. It was essential to the deal," etc., etc. The plaintiff didn't ask him a single question about it. Mr. Rothschild, I imagine, was flabbergasted. He felt, "We need a little record on this, don't we?"

He asked a question at the end. He says to his client—I'm paraphrasing—something to this effect, "Was the common stock option necessary in order for you to agree to this deal?" The client says, "Yes." It's a good job by him to fill that hole [Tr. 70] in the record, because it was embarrassing that it wasn't there, but where were our representatives?

Why weren't they grilling him on that? "You say it was essential? Who did you tell it was essential? You talked to him. Exactly what did you say? Is it in writing anywhere? Maybe I want to talk to these people to see if I can develop a conflict." Didn't ask a single question. Denend's deposition—again, I could never prove it—reads to me like direct examination. You read the deposition, Your Honor. There are an amazing number of questions answered with, "Yes."

That doesn't mean anything in and of itself. But this is a hostile interrogation. It looks anything but hostile. My guess is—I don't know. Nobody would tell me. My guess is there were talks going on at this point, or maybe there was an agreement in principle at that point, by the time the depositions occurred. But please, Your Honor, we would ask you to read these—this record, see whether or not you think this record is really fully developed.

* * *

[Tr. 72] Plaintiffs' counsel talked at great length about this board, how informed it was, etc., etc., etc. It's a four-man board. The third guy, Mr. Abbey, came on the board in March. Maybe he did. Maybe he did get up to speed and was an informed member of this board, knew the company. The deal was signed up May 5th or 6th. It's possible, but I think there is at least a question there. And Mr. Abbey's deposition wasn't taken.

Now from a strategy standpoint—the plaintiffs can plot their own strategy, but you give me the list of directors, and I will pick the guys I depose. One guy I pick is the new guy on the board, because he has been there for a month. I think he [Tr. 73] might be ripe for not understanding this transaction. He wasn't deposed, and counsel stands up here and talks about such an informed board, what a great job. Only four directors. You don't have to depose all the board in every case, but why not depose this fellow? We don't know. Your Honor doesn't know.

* * *

[Tr. 75] MR. SQUITIERI: I would like to respond to Mr. Williams' characterization of my conduct and present my version [Tr. 76] for the Court, which won't take but a minute. That is, I did get a call from Mr. Williams. There were certain things that I did discuss that I did not feel needed to await the signing of a confidentiality order. That's what we thought we got out of the settlement. I advised Mr. Williams as to questions on the settlement negotiations, he should refer to—refer himself to Mr. Arthur Abbey, of the firm, who had those discussions particularly. I am unaware that Mr. Williams ever picked up the phone to call Mr. Abbey. That seems where he has has the most curiosity as to what went on.

As far as the other questions, they are all set forth in the record that was made available to Mr. Williams at my office. He happened to catch me in a two-week period when I was not in my office very much. That explains the fact that the phone calls weren't returned. But has was made aware that Mr. Abbey was competent to answer questions that he had an interest in. As far as anyone can tell, he never picked up the phone to him.

* * *

[Tr. 82] MR. WILLIAMS: . . . Real quick point, Your Honor, but let me say I don't have any recollection of anybody saying to me, "Talk to Arthur." I would have done so. I sent a letter up to Mr. Squitieri after he supposedly told me to talk to Arthur saying, "Please return my calls." I would have thought he would have written back telling me, "I told you. Talk to Arthur." I'm not saying it didn't happen. I'm saying I have no recollection.

* * *

APPENDIX N

Excerpt From "Opening Brief of Appellants-Objectors Below" Before the Supreme Court of Delaware

* * *

By way of further example, no meaningful discovery occurred as to a number of likely outcome determinative issues, including: (1) the understanding, or lack thereof, by the board of Kidder's valuation analyses and its severe limitations; (2) why Kidder's valuation studies differed so dramatically from Salomon Brothers' similar studies, especially the critical disparities in the "comparable transactions" analyses; (3) who was responsible for deleting the material qualifications from Kidder's draft fairness opinion before the sterilized version was disclosed to the shareholders and precisely why those omissions occurred; and (4) why no one contacted the many companies, including Vitalink's competitors and major customers, who admittedly were well aware that Vitalink was for sale.

The proposed settlement is a sham. It is grossly unfair to the shareholders who are being forced to relinquish their fundamental due process rights to pursue their claims in exchange for the truly frivolous consideration offered. The lower court's decision to approve this settlement should be reversed.

* * *

APPENDIX O

Excerpt from "Reply Brief of Appellants-Objectors Below" Before the Supreme Court of Delaware

* * *

Other examples of the half-hearted efforts of plaintiffs' counsel abound in the discovery record. For instance, the critical deposition of Mr. Denend lasted less than three hours and shows no signs of credible adversarial effort. Of the four Vitalink directors, Denend's deposition was one of only two taken. One director, who had been on the board only since March, 1991, was passed over. In fact, despite unanimous board approval of the transaction, Denend was the only director even named as a defendant.

Under these circumstances, it is doubtful whether foreclosure at this time of the shareholders' claims would meet minimal constitutional requirements, let alone Delaware standards of fairness. *See In re Real Estate Title and Settlement Servs. Litig.*, 869 F.2d 760, 769 (3d Cir.), *cert. denied*, 493 U.S. 821 (1989). This settlement meets neither standard and the decision validating it should be reversed.

* * *

APPENDIX P

Excerpts From Transcript of Oral Argument Before the Supreme Court of Delaware

[Tr. 27] MR. SQUITIERI: . . . This was a—recognized as a very weak case, and one that we recognized would have been very, very, very difficult.

JUSTICE HORSEY: And you recognized that within how many weeks of filing suit?

MR. SQUITIERI: Excuse me?

JUSTICE HORSEY: And you recognized that within how many weeks of filing suit?

MR. SQUITIERI: Well, within the space of the depositions.

JUSTICE HORSEY: Within how many weeks?

MR. SQUITIERI: Excuse me?

JUSTICE HORSEY: Within how many weeks?

[Tr. 28] MR. SQUITIERI: I believe it was—

JUSTICE MOORE: About two weeks.

MR. SQUITIERI: About two-and-a-half or three weeks.

JUSTICE HORSEY: So within two weeks or so, you go from a position of euphoria, where you have a great claim, to a position, "Gosh, this is an awful case."

MR. SQUITIERI: But in between, we are informed, Justice Horsey. We are not looking at the same body of information that we were in the beginning. Now, in that two-and-a-half weeks, we find out that the board is, in fact, independent, and we find out that they are, in fact, active and they are not dominated.

* * *

[Tr. 50] MR. CHRISTOPHER: Justice Horsey expressed some

questions. He wondered how is it that a lawsuit that's based on a press release, that can't wait to be pushed into the courthouse door, with all this merit, all of a sudden has no merit. I think it's enlightening to point out that that conclusion was reached after three days of depositions. Now, it was a compacted schedule. There was a preliminary injunction motion.

The two CEOs of the acquiring and acquired company—I would consider certainly the principals in this negotiation—were both scheduled for deposition the same day. Both were done before lunch time. I would commend the Court to reach—I'm sure you have—both deposition transcripts. They are hardly a portrayal of advocacy.

JUSTICE HOLLAND: Well, Mr. Christopher, in view of the merit you attribute to this suit, does the record reflect why your clients [Tr. 51] didn't file one of their own?

MR. CHRISTOPHER: I think it does, Your Honor. This transaction was announced on May 6th, I believe. The tender offer wasn't commenced with the SEC until the 13th. There were a flood of class action lawsuits filed between that period of time, but the suits were filed before we—before my clients had knowledge that a deal was done. The suits were settled before we had knowledge that a lawsuit was commenced. This case only lasted, in essence, less than two weeks.

We are criticized for not coming in and bringing our suit. We are supposedly represented by plaintiffs' counsel, Mr. Squitieri. So my clients were theoretically represented in the lawsuits that were pending. In reality, we certainly were not represented. But that's why we didn't file a suit. This case was settled before any reasonable person willing to file a lawsuit based on investigation in fact could have done so.

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[Tr. 54] It's not rebuttal, Your Honor, but it does tie into

this—Your Honor's questions to plaintiffs' counsel about their ability to evaluate these claims and settle this case in a short time period.

The disclosure claims in this case were never brought. There are no allegations in the complaints in this case filed by class counsel that contain disclosure allegations. There is not one scrap of discovery in this case concerning these disclosure violations. Not one. I don't know how—[Tr. 55] I have a hard time seeing how a responsible lawsuit was filed on the basis that it was filed in this case. I have an even harder time understanding how counsel representing—in a fiduciary capacity, representing a class of stockholders, can evaluate disclosure claims and decide whether to release those claims when it doesn't even have the benefit of discovery to do so.

I don't think that disclosure claims ever occurred to these plaintiffs. I think they are ill-suited to stand here and rebut them.

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